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Build Subscription Revenue

Best Practices for Customer Retention

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Introduction

The true health of any business is closely related to how well it acquires and retains customers. The metrics for these two functions will tell you much more about the long-term outlook of the company than a yearly financial filing. This truth has extra significance for digital businesses, especially those with recurring revenue business models. This guide will discuss the best practices that are most effective in helping digital businesses optimize their customer retention strategy.

Customer retention, simply defined, is the ability for a company to keep its existing customers. It is the measure of a company's ability to provide enough value with its products or services for customers to keep them coming back for more. The critical metric to measure customer retention for digital businesses with recurring revenue is Average Customer Lifetime Value (ACLV). ACLV is the product of the customer duration and the average recurring charge. For example a $15 monthly charge and an average customer lifetime of 20 months results in an ACLV of $300.

The flip side of customer retention is to analyze how and why customers are leaving. You need to fully understand the exit paths that customers may take and develop a strategy to address each one. We will discuss approaches for opt-outs, cancellations, customer service refunds, failed payment methods and chargebacks in more detail.

The main purpose of this guide is to provide advice for how to improve processes. However, improving the processes alone is often not enough. Digital businesses should embrace an approach of continuous improvement to be truly successful. In addition, you need to understand your customers' behavior and demographics. Knowing as much as possible about your customers, how they use your service or product, and how they interact with one another and with your company will provide key insights to understanding the best way to retain them.

One of the simplest ways to determine why customers are leaving is to work with your customer service department to identify the top five support issues. The most common issues should be addressed with specific retention offers used by customer service representatives and also incorporated into the website and self-support. As would be expected, the top reasons are always a moving target and require constant adjustment based on the most recent data.

In addition to continuously improving support issues, it is necessary to communicate to your customers about the changes and enhancements that have been made to your products and services and highlight the value you provide. By communicating new features, content and improvements through email and across your website, customers are more likely to see continued value in your products and stay longer.

The last point to consider before diving into more detail is the security of Personably Identifiable Information (PII). For digital businesses with recurring billing models, data security is even more important as storage of the customer's payment information is required along with their name and address. Privacy standards have been enacted across the globe to regulate handling PII, but the major credit card companies have established additional requirements for uniform protection around this sensitive information, resulting in the PCI Security Standards Council Data Security Standard (PCI DSS). While this standard is a mandate and may appear burdensome initially, there are longer-term benefits to digital businesses. Once customers know that a digital business is taking all possible precautions and has implemented strict security standards, they are more likely to feel comfortable doing business with you, both initially and on subsequent visits. To this end, digital businesses should make it clear that they have achieved compliance and are taking extra steps to protect their customers. With this is mind, the PCI DSS should be considered a baseline to build upon for true data security.

This guide will discuss best practices around these issues and outline specific actions that can help a digital business increase its customer retention. To that end, we will talk about how to measure retention and action plans for the most common exit paths. Later, we will discuss some strategies for handling friendly fraud chargebacks and how pricing discrimination can be leveraged to keep customers engage longer. Finally, we summarize and highlight customer successes on the Vindicia® CashBox® platform.

Measuring Retention

Establishing a Baseline

The first step to improving a process is to understand what success looks like. Identification of the key metrics that track progress towards your goals is critical to measuring your success. Customer retention will vary widely depending on several criteria specific to the business environment and customer demographics. That is why it is important to first establish a group of baseline metrics that includes the makeup of your customer base, typical behavior and usage patterns. Of course, the ability to create baselines is only as good as the data that are available. New functionality may be required to collect more data about your current and prospective customers in order to better understand them.

Several criteria you may want to track include:

Age	Gender
Location	Join Date
Logins / Month	Usage
# of Support Issues	Income
Referral Source	Product
Campaign or Promotion	Trial Participation

Of course, not all retention metrics will be specific to your business. It is important to have general industry-wide metrics such as payment method failure rates, the percentage of failed transactions, and chargeback rates. Payment method failure statistics can be further divided by payment method, card type (for credit card failures), location, currency, and reason codes. Rates and reason codes will vary between processors, and it is helpful to know if the reason codes you are experiencing are common for your processor or if you are receiving more of a certain code than average. It is also useful to look at payment failures by geography and currency to detect regional trends, which can help shape your global strategy. If you are seeing an abnormal failure rate, there may be external factors in your site or processes that are triggering certain payment method failure response codes. Understanding the reason codes and why you are receiving them will be the first step in identifying and addressing these external factors. Overall, examining industry statistics by payment methods and comparing your most successful and most profitable methods against them is a good way to align your business with your peers across the industry.

Business Specific Metrics

As we mentioned initially, the most important metric for a digital business with a recurring revenue commerce model is Average Customer Lifetime Value (ACLV) – a product of customer duration and the average recurring charge. Your specific ACLV will be extremely dependent on your business environment. ACLV reflects not only the price being charged, but also the overall customer demographics, customer behavior and the relative value of your product to your customer. Of the two ACLV components, average recurring charge is the simplest to determine. The average recurring charge can be determined fairly easily by dividing the total transaction revenue during the period by the number of customers and the number of billing periods covered. For example, the average recurring charge for a business with monthly billing periods would be the gross revenue for a given year, divided by the product of the billing periods (12) and the number of unique purchases.

Customer duration however, requires a bit more analysis. The most straightforward method of determining duration is to take a group of customers who started in the same billing period and calculate how many remained at different historical points. To give an example, look at all customers who started in January on a monthly billing cycle and then calculate the number of those customers who still remain at the end of each subsequent month. Once you find a customer drop-off between 80%-90%, depending on other business variables discussed below, the difference between the starting point and the drop-off point will be your customer lifetime. Performing this analysis for several customer groups (cohorts), based on start dates, acquisition method and other factors, will generate an average customer lifetime. These calculations should be done for each product of billing plan that is offered. Usually, different products will have unique customer demographics and therefore a different ACLV.

The other necessary business specific metrics are around cancellations, opt-outs and refunds. The rate at which customers leave is something that will greatly affect your business, industry and customers, and these metrics are obviously of key importance to any understanding of customer retention. Luckily, these metrics are much easier to determine and track.

Customer Exit Paths and Strategies

Cancellations and Opt-Outs

Cancellations and opt-outs are two sides of the same coin. Cancellations occur after an existing customer has a payment failure that cannot be re-billed, whereas opt-outs happen when a prospect or trial customer takes action to leave and explicitly chooses to stop being billed for your product or service. Despite differences between the two, both groups should reflect similar patterns and reasons for leaving.

While digital businesses can optimize their process, improve their product and site and work to establish deeper relationships with their customers, customer cancellations and opt-outs will always occur. For this reason it is important to have a clear exit path for those who truly want to leave. If a clear exit is not established, a greater number of customers will issue chargebacks instead of fighting through a burdensome exit process. Of course, only those trial users who have converted to customers will issue chargebacks, but a clear exit path also prevents unhappy trial users who did not cancel in time from subsequently issuing a chargeback after their trial converts. In addition, having a clear exit path and communicating how to use it shows a confidence in your product and an understanding of how to best treat your customers. Combined with the security of knowing they can leave at any time, showing customers how to leave will actually increase retention while simultaneously reducing chargebacks.

A large software company switched to Vindicia CashBox for our recurring billing capabilities. By taking advantage of our customer retention features, they were able to improve their retention by over 50% while increasing customer acquisition.

An additional exit path that should be discussed here is one for product expirations. When a product offering comes to an end, either from fixed length offerings or due to product end-of-life, digital businesses should issue a communication that gives their customers a path to continue using comparable offerings.

Customer Self-Service

It is equally vital for digital businesses to provide a self-service website for their customers. It should not only be easy for a customer to leave, but for them to update and control their own personal and payment information. Grouping all necessary account functions into one area will help minimize customer confusion. In addition, providing both self-service support options and exit paths on the web are far less costly than via phone support. Exiting via the web is also a more controlled environment for retention surveys and offers.

Cancellation Communication

Once a customer has cancelled, a final communication must be sent highlighting the final billing date and indication that no future billings will occur. For trial customers, a similar communication should be sent if they have chosen to opt-out. Even before that point, prospects should have a chance to receive a trial expiration reminder. This can be as simple as providing a link in your communications or a button on the customer self-service site. This reminder provides additional comfort levels for the same reasons as having a clear exit path.

Customer Service and Refunds

For many, the first line of customer interaction is your customer service department. Customer who are having problems with your product, or those thinking of leaving, will be the most motivated to expend the time and effort to seek out phone support. Knowing this, support personnel would be well equipped to handle frustrated customers, calm them down and work out the problems. In fact, by using a friendly and empathetic approach, digital businesses can not only solve problems but also actually increase customer retention.

The feedback received directly from customers can be used to strengthen products and improve processes. In our Best Practice guide on Customer Communications we talk at length about the power of retention offers and surveys on the web. All of these concepts apply to customer service as well. Work with your customer service department to identify the top five issues and reasons that customer leave. Once the data has been collected, craft specific solutions, scripts and retention offer for each of these issues. If customers still want to leave, ask the same questions used in your online exit survey. Not only will the survey help standardize the data for later analysis, it will offer greater insight into why customers are leaving, regardless of the way they leave.

Retention offers are critical. With a live customer, it is much easier to reason with them and ask if they would be interested in paying a lower price for a portion of the functionality. If they are still leaning towards cancelling, a simple reminder they can always cancel next month may be all it takes to keep them as a customer. For digital businesses with high margins it always makes sense to try and save a sale with a lower cost alternative.

Payment Failures

Up until now, the focus has been on customer-facing improvements. However, equal effort should be spent examining the back-end processes around how transactions are processed. Digital businesses with recurring billing commerce models face a unique challenge with payment failures. Unlike online retail, or other one-time transaction based businesses, subscription-based payment methods must be stored in order to be charged again at the next billing period. When a payment method is processed regularly, it is more prone to failure as payment details may change. For example, credit cards may temporarily be over their limit

Vindicia's advanced billing logic alone has been responsible for significant improvements in customer retention for our ciients. Utilizing only our advanced billing logic, one of our clients was able to improve their customer retention rate from 92% to 98% within a few months of implementation. For digital businesses with a lower starting retention rate, the improvements have been even greater.

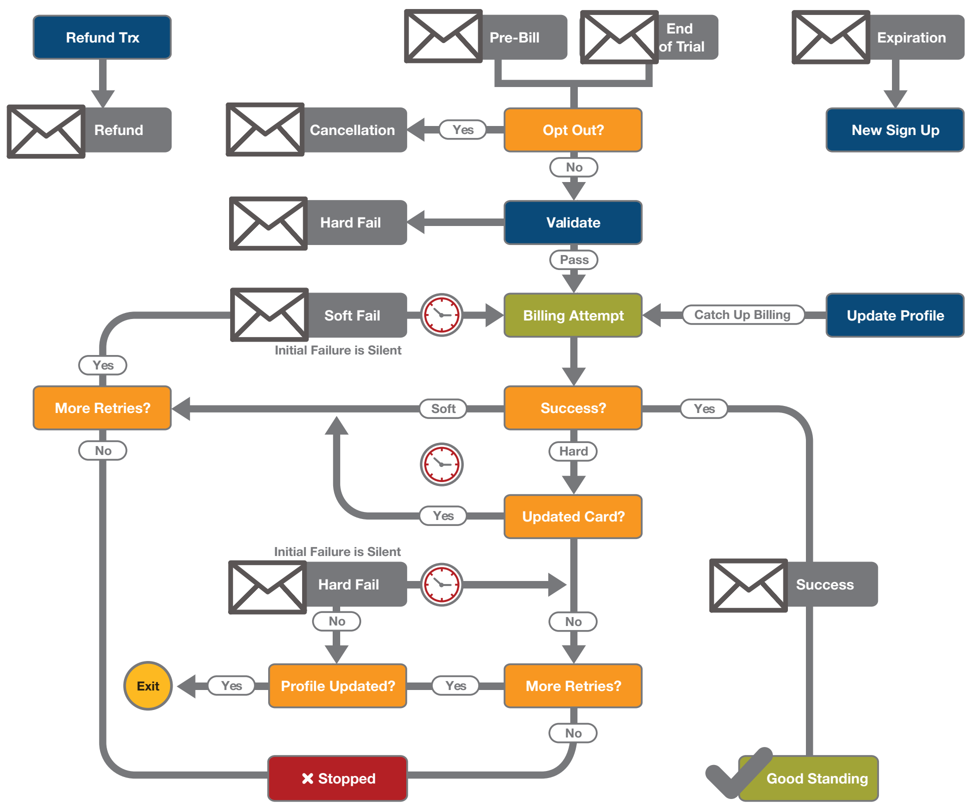
at the time they are processed, they may have expired, billing details may have changed, or the processing network may even be down temporarily. Three clear best practices to follow for payment failures are: 1) Use advanced billing logic and customer communications at each step of the process in order to maximize the number of successful transactions; 2) Track and analyze the reason codes for the failures you are experiencing; and 3) Leverage Account Updater services when available.

Advanced billing logic is, simply stated, attempting to process a transaction again after experiencing a "soft" failure. A soft failure is most easily defined as a failure that can be fixed as opposed to a "hard" failure, which cannot be fixed or re-tried. Payment processors provide a reason code for every transaction processed and that code will indicate whether a failure is "hard" or "soft." As example of a "hard" failure would be a card that has been reported lost or stolen. A "soft" failure example is a card that is valid but over the limit or subject to a temporary processor network outage. Once a soft failure is identified, several steps can be taken to offset that failure. Every digital business will have to decide who exactly they would like to handle each type of failure, but the main concept of attempting transactions again when possible remains the same.

Take payment processor network outages as an example. If a card is rejected because the network is down, simply retrying the card in a few hours or the following day will likely result in a successful transaction without requiring any customer interaction. Temporary credit limit restrictions can be resolved in a similar fashion. A best practice that may not be immediately evident involves the timing of the billing retries. A series of retries should be adjusted so that the attempts are on different days of the week. This especially holds true for hard failures that require additional information from the customer via email. Communications are sent on the same day of the week may not be seen due to the customer's schedule or email volume. To avoid this, simply set the retry and communication attempts for 10 days.

Of course, you need to keep customers notified of issues and work with them to resolve failures when applicable. By carefully communicating with customers at this stage, you will set appropriate expectations that they may have service disruptions, see items appearing in their online credit card statement or need to provide alternative payment methods. This may be as straightforward as sending an email noting issues with a certain payment and directing them to the self-service support site to update their payment information.

The second best practice mentioned is to analyze the failures by the reason codes returned from the payment processor. As mentioned above, the reason codes classify each failed transaction as a "hard" or a "soft" failure, but they also give more information about the details of each failure type. By tracking and analyzing these codes, you will be able to see which codes are the most common for your business and take the necessary steps to correct your processes in the future.



Vindicia CashBox Advanced Billing Logic Flowchart

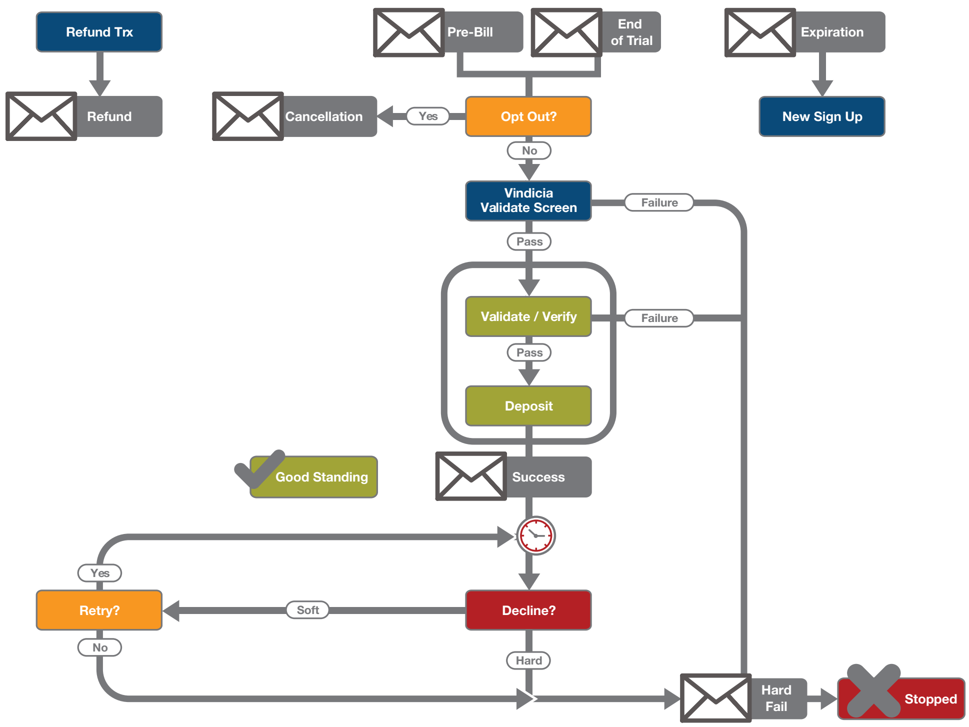
Lastly, certain payment processors offer a feature called Account Updater. This aptly named service offers a fee of all accounts that have been updated by Visa or MasterCard affiliated banks in North America and Western Europe. If a new card is issued, or the card issuer updates a customer's billing information, this data will be pushed out to digital businesses that have processed these cards. This service is very powerful for businesses that rely on recurring billing and typically results in at least a 2-3% increase in customer retention by itself. All digital businesses with a recurring business model should ask their payment processors if they offer this service and take advantage of it as soon as possible.

Preventing Customer Losses Due to Payment Failures

There are a few additional tips that may help prevent losing customers when their payment method fails. The first is to focus on payment method profitability and offer incentives for customers to move from the least profitable, highest failure methods to the most profitable and reliable (e.g. a gaming company may offer a free virtual good or month of service for customers using mobile payment to add a credit card as their primary payment method). Additionally, there will be times when a card failure should not necessarily result in a termination of service. If a customer's payment method fails, the first move should not be to cut off their entitlement, but to attempt to fix the problem even if this entails giving away access for free. It is much more valuable to extend the customer lifetime by giving away an extra 15 days of service than to anger a customer for life.

Alternative Payment Handling

Some payment methods require unique rule sets. Electronic Check Processing (ECP) may be the best payment method for companies selling to other businesses, especially if they are processing large transaction amounts. ECP has much less flexibility with retries than credit cards, but it is possible and mostly happens within the bank network. For digital businesses, it is necessary to factor in a delay and track any unsuccessful responses according to bank timetables.



Vindicia CashBox Routing Flowchart for ECP Transactions

Other alternative payment methods with their own set of considerations are PayPal and “Push” payment methods, such as Western Union or Boleto Bancario (Brazil). For those who are not familiar with Push payment methods, they are payment options that require an offline transaction be process (your customer has to “push” the payment to you) in order to complete a payment. To use the Boleto Bancario example, a digital business presents the customer with an online form that can be printed out with the appropriate account information. The customer then prints or copies the information, travels to their bank and instructs them to transfer funds to the appropriate account. Other Push methods are payable at a variety of locations, but the basic mechanics are very similar. Due to their unique nature and appeal, digital businesses offering these methods will need to consider their retry or reminder schedules and how to handle failures.

Business Process Tip:
Most consumers wait until the weekend to take care of their billing issues. Making sure that your customer service department is staffed on the weekends could have a significant impact on your chargeback rate. If cost is an issue, consider Wednesday through Sunday instead of Monday through Friday.

Chargebacks

Chargebacks occur when a customer, or the acquiring bank, refuse a credit card payment and charges it back to the digital business. Chargebacks can be grouped into three main categories – those that are due to fraudulent activity, those resulting from a company's business processes, and those that happen as a result of a claim that the product or service was never received. While the first two categories of chargebacks can be reduced through fraud screening and business process optimization, the chargebacks that fall into the last category will be the main focus of this discussion. These are referred to as "friendly fraud" – when a customer uses your service and then refuses to pay for it. As expected, this situation is not pleasant for digital businesses. After providing a requested service, not only are they denied payment, but they are also charged additional fees by their payment processor. All, however, is not lost for the digital business. The absolute first step is to stop all recurring billing for that customer in order to eliminate future chargebacks. Turning a customer account off should be done in a way that is easily reversible. The chargeback is more likely to be resolved and the customer more likely to want to continue using your service if their time, effort and status invested in your product or service is not lost.

Regardless of the reason, it will probably be necessary to reach out to the customer in order to resolve the issue. If the chargeback was received due to a process error on your end, the customer should not be penalized. They should be assured the necessary changes will be made and their account restored to good standing if they are amenable. However, if the customer is simply issuing a chargeback because he does not think he will be caught, you should immediately disable access to the product or service. Cutting off access to your product may be enough for them to want to restore their service. They have already proven to be an unreliable customer and many chargebacks will be irresolvable regardless of the actions taken. As a way to recoup costs, you may even want to implement a reinstatement fee that equals the cost of the chargeback fines for users who want to be restored to good standing. Of course, for a customer who has issued one chargeback, issuing a second chargeback later on would be grounds for immediate cancellation and/or deletion of all account information.

Retrieval requests are an important aspect of the chargeback process. These are the inquiries that banks issue to request more information about your company and the products used. Digital businesses only have a few days to respond to these retrieval requests, but it is vital that they do so. Simply responding to the request greatly reduces the chances of a chargeback, while not responding guarantees that a retrieval request will turn into a chargeback.

Another recommended chargeback process is to remarket using reason codes associated with the chargeback. A note of caution is that the reason codes given by issuing banks on chargebacks may not be the actual reasons for a given chargeback. As mentioned previously, it is critical to track why a process is breaking down in order to continually improve the service you are providing. This holds true for chargebacks as well. By correctly categorizing chargebacks by reason code and thus knowing why your customers leave, it is much more likely that you will be able to fix any issues. By collecting customer information and grouping it by reason code, it is possible to use these customers as the basis for a remarketing campaign later on. You may find many of your past customers who left under antagonistic conditions are willing to return after a suitable cooling down period.

Of course, along with resolving "friendly fraud" chargebacks, all chargebacks should be reviewed and potentially challenged. An experienced team of fraud analysts with the right tools should be able to win and recover revenue for at least 60% of "friendly fraud" chargebacks. Many digital businesses are not aware of the amount of friendly fraud chargebacks they encounter due to mislabeled reason codes by the payment processors. If you are not fighting these chargebacks today, or only fighting a small subset of the total true number, you may be throwing away considerable revenue each month.

Price Discrimination

Digital businesses have a clear advantage when selling online with a minimal cost of goods (COGS). This allows tremendous flexibility when it comes to pricing. While there are many reasons to not underprice your goods, there are times when it is advantageous to drop the prices in order to retain paying customers. The main goal of recurring billing is to keep your customers for as long as possible – maximizing ACLV. The most common methods of price discrimination are:

- Retention offers
- Targeted remarketing
- Short-term discounts
- Alternative billing plans

Summary

To improve customer retention, digital businesses need to embrace the entire problem and realize that it requires a continual stream of awareness and maintenance. Each customer exit must be tracked, studied, analyzed and improved. This is a resource intensive, ongoing process, but after you have identified the overall goals of your customer retention efforts and the metrics that will help guide you, maximizing customer retention is much less daunting.

Each exit path should be closely examined so you can identify the appropriate retention strategy for the issues unique to that path. As you implement these strategies, you will find that the benefits ripple across multiple departments. A good example is the customer service improvements mentioned above: If customers are able to make most changes themselves via a self-service website and the support representatives are better armed to make a difference by retaining more customers, not only will their internal metrics improve, but morale internally and in your customer base will as well. In addition, many digital businesses only worry about chargebacks with respect to imposed acquiring network limits (e.g., the Visa 1% rule) and overlook the revenue recovery options associated with friendly fraud chargebacks.

By looking at the overall picture of how customer retention fits in with your website, many opportunities present themselves to improve customer retention. The problem typically is not where to improve, but which issue to fix first. Hopefully, this paper offers key areas to focus on and sparks ideas on how to craft your strategies.

The Benefits of Vindicia and CashBox

Our marketing and selling automation solution helps digital businesses improve their customer retention by allowing the necessary flexibility to communicate with customers, intelligently process payments with advanced billing logic, arm customer service with the tools to satisfy customer and enable support for powerful customer self-service websites. Combined with pre- and post-transaction fraud management to reduce true fraud transactions and recover revenue from friendly fraud chargebacks, Vindicia CashBox offers a complete customer retention solution. To provide peace of mind to our digital businesses and their customers, our solutions are certified to the highest levels of PCI DSS and SSAE 16 compliance. This ensures you never have to worry about customer payment information being exposed. Trust and reliability are equally important to us – our digital businesses use our infrastructure to handle over 400,000 transactions each day all over the globe in dozens of currencies and more than 35 languages – totaling more than $4 billion processed on our platform.

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About Vindicia

Vindicia, the true leader in enterprise-class subscription billing, was recently ranked the Number One billing software solution on the market by Billing Software.com. Vindicia takes subscription billing to new levels.

Vindicia CashBox combines cutting edge customer acquisition methods with advanced customer retention technologies, while maintaining unmatched scalability and 99.99% up-time. Vindicia has processed more than $6 billion globally and generates over $90 million in annual incremental revenue for clients. Our clients include TransUnion Interactive, Intuit, Activision Blizzard, IAC, Bloomberg, Vimeo and Next Issue Media. To learn more, visit www.vindicia.com, connect with us on Twitter (@vindicia), Facebook, LinkedIn or read the blog at blog.vindicia.com.