THE ROLE OF TERMINATION FEE COMMITMENT IN DEVELOPING CUSTOMER VALUE IN THE TELECOMMUNICATION INDUSTRY: AN EMPIRICAL STUDY

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Abstract

This study focuses on the marketing variable Termination Fee Commitment and its relationship with customer value. The use of this variable is very extended in different industries for its influence on customer retention from the moment of acquisition. Strikingly, there is very little research in this topic.A large customer database of a telecommunications company containing five years of information about 63,165 customers is used for this purpose. Linear regression and ANOVA methods are applied for the analysis.

Results of the empirical analysis indicate that the application of a termination fee commitment has a positive impact on customer retention and customer value, with no negative impact on customer satisfaction.

Keywords: customer value,retention, market orientation, penalty, discounts

Introduction

The change from a product orientation to customer orientation has long been interpreted by companies, specifically in the telecommunications sector(but also in many others), as an "everythingfor the customer" (Reinartz and Kumar 2002). Everything to acquire and retain customers In the Spanish market large telephone companies have subsidized telecom equipment on this purpose since late 90's. With this strategy Spain has become a world leader in smartphone penetration and internet access from smartphones (OECD 2015).

These commercialplans cost the Spanish companies hundreds of billions of euros (CNMC 2014) and promoted a customer's change of service provider well above the European Union mean rate (60 percent of Spanish customers have changed operator compared to European Union's44 percent -Eurobarometer 2014-).In any case, switching of telecomm service provider is a common practice, and the churn rate (cancellations caused by a change to another company) stands above 25 per cent per year in mature markets other than the European (Wong 2011).

The Spanish operators (in particular the two largest, Movistar and Vodafone) have recognized the unsustainability of this model and have stopped the 100% subsidize of mobile phones, changing their strategy to putthe efforts on the customer base (CNMC 2014).

How could companies maintain the acquisition and at the same time retain customers? It is very common, even in big enterprises, that the areas of marketing, customer retention and customer recovery are in separate departments, with different objectives and independent strategies (Thomas 2001). This situation is a consequence of a widespread idea in business: acquisition and retention are independent processes (Thomas *et al.* 2004). This assumption distorts the ultimate goal of marketing actions, which should be to generate value for the company (Connor 2007). By contrast, a market-oriented company should consider that working retention and customer acquisition as a whole, not separately, increases customer perceived value through strategies focused in managing a profitable portfolio (Ketchen*et al.*

2007).

To unify acquisition and retention processes and budgets marketing managers must design strategies that increase customer value by dealing with different marketing variables jointly (Cronin*et al.* 2000). On this line, the variables included in the commercial offer must be regarded as key variables not only for acquisition but also for retention. These are the basis of the trade between the company and the customer, and therefore they are the starting point of their relationship (unlike switching costs, which become evident when the customer is ready to reckon a change of supplier -Yang and Peterson 2004-).

In the telecommunications field, three offer variables and their affection to customer value have been extensively investigated:price (Yoon *et al.* 2014), discounts (Mohan*et al.*2015) and bundling (Jiang*et al.*2011). The termination fee commitment (TFC), despite its widespread deployment in the global telecommunications industry (Eurobarometer 2014) has very little presence in the literature.

This research addresses the following questions: does the TFCincrease customer lifetime in the company? It's inclusion in the offer affects sales? Does it generate more profitability to the company? How does it affect customer satisfaction?

Theoretical framework

The TFCis used by most operators to ensure that the customer will not go to the competence before the amortization of the economic advantage offered (discounts) or ofthe equipment given at low cost (usually cellulars, smartphones or modems -CNMC 2014-).

It includes three elements: the commitment of the customer (contract length), the gift offered by thecompany as compensation and the penalty. Together they make up the *tradeoff* that the company offers to the customer in which the customer gains an advantage in price or quality of service in exchange for a narrower commitment to the company (Kim 2007). At the same time, the company reinforces the commitment with a penalty for non – compliance (CNMC 2014).

The commitment is a legal element that enters into a commercial transaction, which is based on trust between the parties (Karjaluoto*et al.* 2015).Trust is the subjective belief that the selling party will fulfill its transactional obligations as understood by the average consumer (Eakuru and Mat 2008). It has a positive effect on purchase intentions and at the same time, a negative effect on the perception of risk (Kim *et al.*2008). With this commitment the company and the customer set the foundation for a relationship. The company can use the commitment to extend the customer lifetime in order to increase its value (Biswas *et al.* 2015).

To make that commitment more attractive, the company can use gifts and discounts. The findings related to neuroscience have shown that people prefer the immediate benefits even if the situation worsens over time because the future costs are generally underestimated (Bar-Gill 2012). And customers are usually more sensitive to promotions consisting of lower prices that those who bet on an improvement in the quality of the product or service (Yoon *et al.* 2014).

Several studies indicate that the existence of discounts increases customer retention (Thomas *et al*. 2004, Jiang *et al*. 2011) and that the difference in the amount of the discount has a greater impact on acquisitions than on customer's lifetime and value (Lewis 2006).To increase customer value with a long-term discounts strategy, it should be noted that the effect of price discount on customer loyalty is related to the relational investment made by the company (Vogel *et al*. 2008). The higher the discount, thegreater the spendingof the customer in the service (and vice versa) which will strengthen customer loyalty (Wong 2011). Also, if the company is able to offer customers a high complementarity in the components of a

product (*bundle*) there is no need to emphasize the discount because the complementarity mitigates the impact of discounts on loyalty (Jiang *et al*. 2011).

The question on the doorstep is (Neyland*et al.*2013): why do companies include penalties to reinforce the commitments? Price is the primary factor when subscribing an Internet Access for users in the EU (Eurobarometer 2014). To compete, companies should then offeradditional services and features, company's image or customer service (Kumar *et al*. 2011). Innovative services, such as those offered by technology companies, involve substantial investment. To recover the investment and also to generate profit, acquisition offers should contain variables that facilitate customer retention in the company and thus guarantee a return on investment (ROI) and a positive customer lifetime value (CLV) -Lewis 2015-.

The studies carried out on the penalties for breach of service show that customers do understand that penalties can be fair when a contract commitment is breached (Fram and McCarthy 1999, Kim 2007, Park and Jang 2014).

Nowadays consumers face many different kinds of penalties: service cancellation fees, late fees, payment for reprint tickets, non-payment penalties, etc. Penalties are imposed rates to customers who break their acquisition agreements(Kim 2007). For its negative character, the execution of the penalty tends to generate negative reactions in the consumer(Fram and McCarthy 1999). It is extremely important to understand customer perceptions, because negative responses (dissatisfaction) usually have greater impact on the results of the companies than positiveresponses (satisfaction) -Kim 2007-.

Fram and McCarthy (1999) studied a group of associates of a consumption entity and observed that theydo not perceive all penalties as unfair and that they are willing to accept their responsibility for failing the terms of the contract. The penalty is considered fair when compensates losses caused by the breach and unfair when it is perceived just as an enrichment(Park and Jang 2014).

To assess whether the sanctions were effective for the consumer compliance with the agreement or not, respondents were asked if the fact of paying a penalty made them feel more obligated to complete the transaction agreed. Sixty percent agreed that the existence of a penalty promotes engagement (Fram and McCarthy 1999).

For Kim (2007), customer perceptions on penalties are at three levels of response: cognitive (perception of justice), affective (emotional response) and behavioral (intention of spreading word of mouth). Knowing these impacts, the company can work on how to influence on customer perceptions.This may mean that the careful application of penalties can be used by the company to recover from financial damage caused by a customer, without impact the recovery to the entire customer portfolioKim (2007).

Kim (2007) concludes that companies using penalties as a defense mechanism should clearly explain them to their customers rather than occult them.According to this study, companies use penalties in these situations:

- as a way to increase revenue. This strategy is proven among financial institutions whose penalties have been increasing in recent years (e.g. surcharges for late payments of credit cards),
- to prevent their customer behaviors harmful for the company by minoring productivity (e.g. ticket re-prints),
- to turn away customers who are not interesting for the company, to focus on more profitable ones. For example charges that some financial institutions apply to customers who do not maintain a minimum monthly balance,
- to recover from economic losses (for example last minute cancellations).

The reason why companies use TFCis crystal-clear. The question that arises is: Is the use of TFC worthwhile for business?The aim of this research is to understand to what extent the

existence of a TFC reinforced with a penalty, impacts on costumer value. Transparency in communication with the customer activates his/her emotions reducing uncertainty in the acquisition process and increasing confidence in the company. It also covers initialexpectations and helpsgenerating good relations between the customer and the company from the beginning (Karjaluoto*et al.* 2015).

At the same time the penalty acts as a barrier to customer cancellation (Park and Jang 2014). The economic cost of change is too high for the customer to justify churn to another company(Yang and Peterson 2004). From the first moment on, it is assumed as part of a deal with the company and the customer lives the service experience in the same way that a customerwith no commitment does (Karjaluoto*et al.* 2015).When the term of the commitment ends, the customer maystart looking for the service supplier with the lowest price, since the economic costs of change have decreased (e.g. when the contract period ends and, therefore, there is no penalty to change)-Yang and Peterson 2004-. By that time, the business should have made the customer feel enthusiastic about the company, in order to avoid cancellation(Thomas *et al*. 2004).

According these previous studies, the following hypotheses are formulated:

H1. *The use of termination fee commitment allows the company to achieve a longer customer lifetime. The longer the duration of the contract that includes a termination fee, the longer the customer lifetime.*

H2. *The longer the duration of the discount included in the trade off, the longer the customer lifetime.*

H3.*The value of a customer with a TFC depends on the investment done in the tradeoff offered by the company and the customer lifetime.*

H4. *Customers with TFC have an equivalent level of satisfaction than customers with no TFC.*

H5. *The existence of a penalty does not affect negatively acquisition as much as the discount affects positively acquisition.*

An empirical research is conducted to provide further information on this topic.We have not found a previous study of this variable related to customer value.

Data and methods

The empirical analysis investigates the relationship of the marketing variable TFCwith the variables customer acquisition, customer lifetime, customer satisfaction and customer value.

The choice of the telecommunications industry for conducting this study is not casual. The high number of cancellations in mature markets (Eurobarometer 2014), have led companies to increase switching costs trying,at the same time,to maintain the number of new activations. The study is conducted on the database of amultinational telecommunications operator that provides wireless internet access and phone calls.A longitudinal study of customer behavior during a five year period is carried out in order to show how customer lifetimeis affected by theTFC.Longitudinal studies related to customer retention are still very limited in the literature (Jiang *et al.* 2011). The interest of this kind of studies is to capture the variations caused by the passage of time and its effect on the results of the company (Kumar *et al.* 2011). This type of studyconstitutesa relevant contribution to the literature itself (overcoming the limitations of cross-sectional studies).

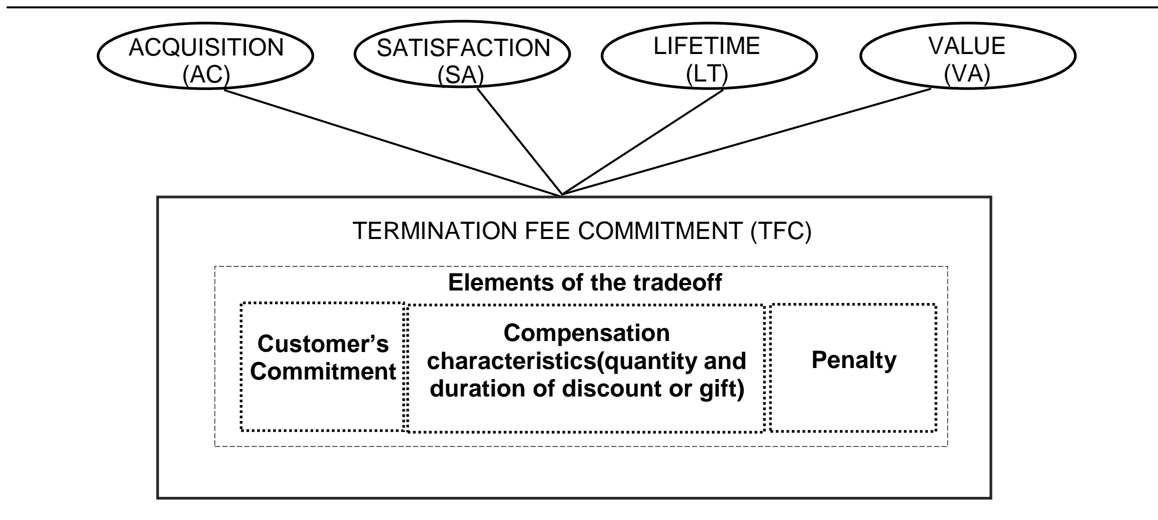
The total number of valid records is 63,165 contracts. The database contains:

- The price contracted by the client
- The conditions agreed: if the customer has a TFC or not and during how long
- Gifts and/or discounts applied and their duration
- The dates of activation and cancellation (and thus customer lifetime).

From the data analysis and the comparison of different offer designs (with or without commitment, with long- or short-duration discount, with a low or high economic penalty), we intend to understand how offer configuration affects customer lifetime and value.

The relations between the TFCand four relevant marketing variables are shown in Figure 1.

FIGURE 1
Relations of the variable Termination Fee Commitment (TFC)



For the purposes of this research, these variables are defined as follows:
Acquisition (AC).Number of activations that occur over a period of time for a particular typeof offer (with or without TFC, with or without discount, etc.).
Satisfaction (SA).It is measured via Net Promoter Score obtained in a survey to customers. Includes two questions: one on whether to recommend the service (yes or no) and another one about the level of recommendation (0 totally unrecommended, 10 absolutely recommended).
Lifetime (LT).This is the period during which the customer service is active in the company.It is measured in number of days.
Value (VA). Income generated by the customer minus discounts (or gifts) of the tradeoff. It is obtained by adding the activation fee, the monthly fee (in daily calculation), the penalty perceived in case of cancellation before the end date of the contractis reached and subtracting the discounts.It is measured in euros.
TFC.It consists in a tradeoff which contains a contract length (the commitment), a compensation (in this analysis is a discount or a gift) and a penalty (in this business, an early termination fee)to reinforce the commitment. It is a variable of the commercial offer which existence may affect or not these variables: acquisition (AC), satisfaction (SA), customer lifetime (LT) and value (VA).

Data collection and analysis

Two databases and methods are used. A) The total customer base of the company is used to analyze the relationship between the TFC and the variables acquisition, lifetime and value, B) A survey done over the 6% of the total customer database is used to analyze the relationship between the TFC and the variable satisfaction.

For the analysis of therelationship between the TFC and the variables acquisition, lifetime and value the original customer data base is modified according to the following criteria: activations of the last year of the period studied(1,180) and customers with retention discounts (1,230) are removed to avoid interference in lifetime and value ratios. The resulting database contains 60,755 records.To calculate the value of customers, we add the activation fee, the monthly fee and the penalty perceived in case of cancellation before the contract length has finished (early termination fee). And the discounts are subtracted.That is, the Past Customer Value is used, since the aim in this study is to analyze the impact of the TFC on the value generated by the customer (not to calculate its future value: CLV).

The TFC consists of three elements: commitment, compensation and penalty. Together they make up the tradeoff between the company and the customer.The variables of each of these elements analyzed in this research are:

1. The commitment.It´s a contract length and its durationranges 0 to 18 months.
2. The compensation. In this research is a discount or a gift and is part of the price. It includes:
   - Activation fee. It can exist or not, and goes from ranges €0 to €120.
   - Monthly fee. It is in all cases €30per month.
   - The quantity of the discount or gift. The total quantity goes from 20€ to 120€.
   - The duration of the discount. A discount is applied in the monthly fee during a period.Ranges from 1 to 12 months.
3. The penalty. In this business is an early termination and ranges from €30 to €250.

The elements are analyzed separately to see their impact on satisfaction, purchasing, lifetime and customer value.

The analysis of the relationship between the TFC and the variable satisfaction is done with asurvey on customer satisfaction carried out by the company.The survey is based on 4,883 phone calls to customers along one year.After removing 1,234 records of customers contacted that did not want to participate we analyze 3,649 customer responses.The sample selection was randomly made by the management tool (ATLAS) installed on the company's call center.

After calculating the probability of error in the sample, it is verified that the sample is representative. The sampling error for a confidence level of 95.5% (2σ) is ± 1.94%.
To contrast both analyses the software IBM SPSS Statistic, version 22, is used. The statistical techniques are detailed in Table 1.

Table 1. Hypothesis and statistical procedure

Relations	Hypothesis	Statistical techniques
Hypothesis relating TFC and Customer Lifetime	**H1. The use of TFC allows the company to achieve a longer customer lifetime in the company. The longer the duration of the contract that includes a termination fee, the longer customer lifetime.**	a) T de Student + Bootstrap b)ANOVA +Bootstrap +Test HSDTukey
	H2.The longer the duration of the discount included in the trade off, the longer customer lifetime.	T Student +ANOVA + Test HSD Tukey
Hypothesis relating TFC and Customer Value	**H3. The value of a customer with a TFC depends on the investment done in the tradeoff offered by the company and the customer lifetime.**	ANOVA + Test HSD Tukey + Linear Regression
Hypothesis relating TFC and Customer Satisfaction	**H4.Customers with TFChave an equivalent level of satisfaction than customers with no TFC.**	Test Chi-square +TStudent +ANOVA
Hypothesis relating TFC and Customer Acquisition	**H5.The existence of a penalty does not affect negatively acquisition as much as the discount affects positively acquisition.**	Linear Regression

Results

The results of the contracts of the variable TFC with the variables customer lifetime, value, satisfaction and acquisition are included in Table 2.

Table 2. Results on contrasts between TFC and customer's lifetime, value, satisfaction and acquisition

Contrast	Test	Variable	TFC	N	Mean (CI 95%)	S.D	Test Studentfor MI			C I95%	Bootstrap		R^2	Anova 1 factor			Test HSD Tukey	R^2
							t	gl	P		Mean Diff.	P		F	gl	P		
Customer lifetime depending on TFC (H1)	TStudent	Lifetime (days)	*No*	6239	375.94	266.17	14.51	60753	.000**	47.40 – 62.20	54.80	.000**	.003					
			Yes	54516	430.74	284.32												
Customer lifetime depending on contract length (H1)	Anova	Lifetime (days)	*No*	6239	375.94	266.17								95.31	3 ; 60751	.000**	(No P = 6-9M) < (12m = 18 m) **	.005
			6-9 months	2364	381.67	202.26												
			12 months	13578	434.29	344.81												
			18 months	38574	432.49	264.07												
Customer lifetime depending on the existence of a discount (H2)	T Student	Lifetime (days)	*No*	28281	417.36	304.87	6.30	60753	.000**	9.99 – 19.01	14.50	.000**	.001					
			Yes	32474	431.86	262.28												
Customer lifetime depending on the duration of the discount (H2)	Anova	Lifetime (days)	*No*	28281	417.36	304.87								111.49	4 ; 60750	.000**	(12m = 3m) <(No = 1 ó 2 m) <6 m **	.007
			1-2 months	4963	427.50	231.60												
			3 months	8911	383.80	248.12												
			6 months	18600	456.39	273.09												
Customer value depending on discount value (investment done in the TFC's tradeoff) (H3)	Anova	Value(€)	*Nodiscount*	18296	426.15	324.02								236.5	5 ; 54510	.000**	(Gift= 90) <(20 = 40 = 60) <doesn'thave **	.021
			20 -30€	5330	378.75	229.24												
			40 - 50€	2087	333.47	226.12												
			60 €	19834	383.23	275.26												
			90 €	4713	308.53	271.49												
			Gift 120€	4256	297.65	259.16												
Customer value depending on customer lifetime (H3)	Linear regression	Predictor factor	Coefficient B	E.T. (B)	CI 95% of B		T-value	P-value	R	R^2								
		Lifetime (days)	0.996	.001	0.994 – 0.997		1184.9	.000**	.984	.963								

Contrast	Test	Variable	*TFC*	N	Mean (CI 95%)	S.D	Test Studentfor MI t	gl	P	C I95%	Bootstrap Mean Diff.	P	R^2	Anova 1 factor F	gl	P	Test HSD Tukey	R^2
Customer satisfaction depending on TFC (H4)	T StudentAnova	TFC	*No*	164	6.70	2.66												
			Yes	3485	6.87	2.59	0.83	3647	.408 NS	N.S.	0.17	.409 NS	.000					
		Contractlength	*No*	164	6.70	2.66	0.23	3 ; 3645	.876 NS	N.S.	--							
			6-9 months	48	6.88	2.29							.000					
			12 months	251	6.88	2.76												
			18 months	3186	6.87	2.58												
	Test Chi-square			*Recommendstheservice*				Chi²	gl	P	R^2							
				Yes		*No*												
		TFC	*No*	79.8% (130)		20.2% (33)		0.25	1	.620 NS	.000							
			Yes	78.1% (2716)		21.9% (761)												
		Contractlength	*No*	79.8% (130)		20.2% (33)		2.04	3	.565 NS	.000							
			6-9 months	70.8% (34)		29.2% (14)												
			12 months	76.9% (193)		23.1% (58)												
			18 months	78.3% (2489)		21.7% (689)												
Customer acquisition depending on penalty and discounts (H5)	Linear regression	Predictor factor	Coefficient B	E.T. (B)		CI 95% of B	T-value	P-value	R	R^2								
		Penalty (€)	2.8×10^{-5}	2.2×10^{-5}		-1.5×10^{-5} / 7.1×10^{-5}	1.30	.195 NS	.005	.000								
		Discount (€)	1.0×10^{-3}	2.7×10^{-5}		9.2×10^{-4} / 1.0×10^{-3}	35.63	3×10^{-275} **	.143	.020								

N.S. = No significant (P>.05) ** = Significant 1% (P<.01)

As shown in Table 2, customers with TFChave a 13 per cent higher lifetime average than customers without TFC, which is significant. This result confirms the first part of Hypothesis 1. Introducing the variable contract length (6-9, 12 and 18 months) the means of customer'slifetime with no termination fee or with reduced contract lengths (6 to 9 months) are clearly lower than the means of those with 12 or 18 months commitment. The number of cancellations decreases when increasing contract length.These results confirm the second part of Hypothesis 1: the use of TFC allows the company to achieve a longer customer lifetime in the company.

The outcome of the discounts analysis shows that customers with long duration discounts (6 months) linked to a TFC, are the customers with the longest lifetime in the company: 9 per cent more than customers with no discount which is significant and confirms Hypothesis 2:the longer the duration of the discount included in the trade off, the longer customer lifetime.

For investment, it is used the total discount variable by assigning a monetary value to each of the discount levels (no discount = 0; 20€ to 30€ = 25; 40€ to 50€ = 45; 60€ = 60; 90€ = 90; more than 120€ = 120 and finally "gift" = 120).The results show a tendency for customer value to decrease as the discount (investment) increases. And the HSD Tukey test clearly states that contracts with discounts over €90 are those with lower customer value.The relationship between customer value (in €) and lifetime (in days) is estimated using a linear regression method and shows that the increase in customer value is almost €1 per day of lifetime in the company. These results confirm Hypothesis 3: The value of a customer with a TFC depends on the investment done in the tradeoff offered by the company and the customer lifetime, and show a difference of 14 per cent in customer value between customers with TFC and customers without this variable in their offer.

The satisfaction variable is contrasted with two dependent variables: 1) question about the recommendation service to family and friends (dichotomous variable: Yes / No) and2) question for a numeric value (0- 10) to quantify this recommendation and hence, the level of satisfaction. As shown in the results, in both cases the rate of subjects that would recommend the company (and therefore it is deduce, are satisfied) is close to 80 per cent in customers with or without TFC. The observed differences between them are not statistically significant.Therefore, the results support the Hypothesis 4 of independence between customer satisfaction and the existence of a TFC in the service contract.

The linear regression methodis used to relate the acquisition with the predictorspenalty and discount to analyze the assumptions related to the effects of TFC on customer acquisition.Results indicate that there is no correlation between acquisition and penalty. Therefore this variable does not affect the acquisition and H5 is contrasted.

Discussion and conclusions

The results of this research show that the TFC is a variable that serves to attract and retain customers generating profitability to the company without a negative impact in customer satisfaction.

When there are high switching costs, the risk of losing the customer is low. But those switching costs can get neutralized by external forces (Yang and Peterson2004). The consumer experience in the sector, the companies themselves and the market regulations, may decrease customers switching costs to change. Two examples are:a) when regulation permits to take the telephone number to another operator, or b) when a bank offers itself to do the administrative formalities to direct debit receipts. In this case, the new bank prevents the customer having to address relational costs when changing service provider. Those situations are used by companies to facilitate competitor's churn (change form one company to another) and its own acquisitions (Biswas *et al.* 2015).

In these cases, the company may consider establishing some variables in the purchase offer to increase switching costs. The variables of the offer are a group of variables that define the conditions under which the service is provided and one of its objectives should be to obtain greater customer engagement with the company (Eakuru and Mat 2008). Its existence, nonexistence and design have impact in the relation acquisition – customer lifetime – benefits (Vogel *et al.* 2008).

The TFC is a cross variable that affects acquisition, it is a switching cost that retainsdeactivations, and it also formalizes an emotion: the engagement (Kim *et al.* 2008). This is the reason whyoperators are interestedin using it(CNMC 2014). It consists of a tradeoff between customer and company with the following elements:

1. A customer commitment to remain in the company during a period (minimum customer lifetime).
2. A penalty (early termination fee) to reinforce the commitment.
3. A gift as compensation to the customer commitment (gift, discount, higher performance, etc.)
4. A transparent and clear communication with the consumer of all these elements. The company must ensure that the consumer has perfectly understood the tradeoff in order to ensure customer satisfaction will not be negatively affected (Kim 2007).

Types of effects of the composition of the variable TFC include a) effects of the penalty on the acquisition, satisfaction, customer lifetime and customer value; and b) effects of the commercial offer on the acquisition, satisfaction, customer lifetime and customer value.

Effects of the penalty on acquisition, satisfaction, customer lifetime and customer value.Penalty in the TFC is an element to reinforce an agreement reached by the parties in exchange for an advantage for each of them. Is this reinforcement necessary? Consumers agree that the existence of penalties is a factor that promotes engagement with the agreement (Fram and McCarthy, 1999).

It is important for the company to know that consumers do not always consider unfair penalties and accept to assume them when they have to (Kim 2007). Certainly when implemented, penalties generate dissatisfaction (Park and Jang 2014). In the study of Fram and McCarthy (1999) 77 per cent of respondents say that the existence of a penalty is a minus when making the decision to acquisition and 60 per cent said that in the future would never again hire a company that charged a penalty.

However, there is a significant difference between acquisition intentions and actual behavior (Seiders *et al.* 2012, Fram and McCarthy 1999). In the present study it is found that the penalty does not affect the acquisitions:

- 90 per cent of the portfolio chose an offer with TFC even when the economic advantage is low (30€ of activation free for a contract length of 12 months).
- Sales tripled using an offer with a penalty amount three times higher, but including a higher monthly discount than other with low penalty and low discount.

When perceived value is high, the penalty reduces its negative impact on the tradeoff (Yoon *et al.* 2014).Customers accept penalties as a concession to do because they believe that the goods or services of the company are differentiated (Jiang *et al.* 2011). In a competitive context in which all companies apply similar service, pricing and policies, the consumer demand will shift to the company that does not apply cancellation penalties (CNMC 2015).

If consumers consider penalties as a negative factor, why firms use a TFC that includes them? These are four main reasons:

1. With the TFC the company guarantees a minimum customer lifetime, enough to at least return the investment done in the acquisition.

2. It is also a powerful acquisition tool, including discounts, gifts, and even the absence of the early termination fee as promotional hooks.Ensuring simultaneously a certain profit to the company.
3. By including in the design an economic switching cost, it is an important tool of customer retention. During the minimum contract period the operator has the opportunity to work in other variables that affect customer loyalty and customer value.
4. The generalization of this practice in the industry, and its transparent communication to consumer (actions in which operators have worked a lot in recent years – Eurobarometer 2014-)avoid customer to feel unsatisfied just because of the type of contract purchased.

In order to avoid negative perceptions on penalty, it must be accompanied by an advantage that combines the desired and the received values(Woodruff 1997). If communication is transparent to the consumer, the consumer accepts the penalty as part of a possible breach of the agreement (Kim 2007). If both parties understand and sign the agreement, customer satisfaction should not be affected, as shown in the results of this investigation.

Effects of the commercial offer on acquisition, satisfaction, customer lifetime and customer value.The TFC is a key variableon a market orientation strategy (Connor 2007). It implies for its design that marketing managers balance its impact on acquisition and retention. How will the amount of penalty affect purchase? How will the discount duration affect customer cancellation? How will a commitment affect customer satisfaction? And finally, how willa TFCaffect customer value?

This research has tried to answer these questions. The results on the investigation show that:

- Customers with TFC stay longer in the company and their value is higher than customers who have no commitment. Customers who chose the offer with TFC have a customer lifetime 13 per cent longer than those who did not, and have a 14% higher value.
- As duration of the commitment increases, also increases retention. But activations decrease. The contract length included in the TFC at the time of acquisition, has effects on purchase and on customer lifetime. The greater commitment, greater lifetime but lesser new acquisitions. The 12 month period of contract is the best valued by customers when purchase.
- Satisfaction is not affected by the existence of TFC.Customers with TFC and those who do not, have considered alike to recommend the service (both 78%) and they have value it with the same value (both 6.3 over 10).
- The TFC acts as a barrier to deactivations and reduces churn. Churn rate decreases when increasing customer's commitment. The existence of a TFC reinforces the relation of the customer with the company. The penalty acts as a barrier to churn, leaving the company time to work on customer´s loyalty.
- The penalty amount (early termination fee) does not affect customer acquisition nor customer lifetime.

TFC included in the acquisition offer helps to keep customers in the portfolio during a minimum period of time to ensure a return on investment and to let the company work on customers' loyalty. But it is only one of the variables on which the company should work to generate long-term value(Kumar *et al.* 2011).

Considering that customer acquisition, retention and recovery areas are not watertight compartments, but interrelated areas, leads to work all marketing variables as part of a unified strategy of the company (Cronin *et al.* 2000).

It is therefore necessary to consider the customer's lifetime as a whole. A lifetime in which the company can take actiondesigning customer relationship strategies that lead to a positive perception of value for both parties: value for the customer and value for the company.

Managerial implications

Managers in the telecommunications sector already use de TFC to attract and retain customers. But there are still practices in order to hideits use or the use of other limitations of the serviceto customers: more than 20 per cent of EU citizens still think it is difficult to compare bundled offers and only 29 per cent of Europeans belief it is easy to make this comparison (Eurobarometer 2014).

Executives should know that this is not only harmful for the company, but also unnecessary.This study shows with empirical results, that customers accept penalties perceived as fair (Kim 2007) and that customers who accept TFC stay more time and are more valuable for the company, without affecting customer satisfaction.

Marketing managers also from sectors other than telecommunications, can use TFC by applying its various elements (contract length, penalty and compensation –discounts, upgrades, gifts-) as a fair *trade off*between the company andthe customer, with transparency and focused in obtaining the highest customer value for the company.

Limitations and further research

The investigation was conducted on Spanish customers of a multinational company with presence in countries of the US, Europe, North and South America. Despite the limitations resulting from the idiosyncrasies of each place is notorious the implementation of TFCs in countries around the world (OECD 2015). Therefore, the results could be extrapolated internationally. As a future line of research, it would be interesting to study how this variable behaves determined by culture and consumer habits in other countries.

Regarding the features of the service, the operator in study offers a product with singularities as no need for fixed line, which attractsa type ofunstable consumer. The results are surely affected by this feature. Customer profile studied is particularly prone to churn (almost half live in rent compared to 17 per centrate in Spain) and 82 percent have no telephone line, compared to 22 percent Spanishrate. This suggests that the data would be even more favorable to the company in the case of a telecommunications operator with traditional services (fixed and mobile telephony and ADSL for example).It would be an interesting line to investigate further.

Finally, TFCs are used in sectors other than telecommunications: tourism, banking, insurance, transport, etc. that are interesting fields of analysis with its own characteristics.

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