

## FEE-BASED ONLINE SERVICES: EXPLORING CONSUMERS' WILLINGNESS TO PAY

L. Richard Ye  
Yue "Jeff" Zhang  
Dat-Dao Nguyen  
James Chiu

California State University, Northridge

### ABSTRACT

*Many online service businesses are beginning to charge fees for services that they used to provide for free. It is unclear whether consumers are ready to embrace this practice. This study explores consumer attitudes toward fee-based online services. The results of the study indicate that consumers' willingness to pay for online services is likely to be influenced by their perceived value of convenience these services provide, and by the extent to which they utilize these services. While consumers appear more willing to pay for services that are qualitatively better than free services, there is also indication that the belief remains strong among many that online services that were free in the past should remain free.*

### INTRODUCTION

During the Internet "gold rush" of the late 1990s, the electronic commerce industry had focused on attracting new customers and expanding market shares by providing advertiser-supported online services free of charge. It has since been argued that providing free online services and relying exclusively on advertising revenues is a business model that is not sustainable (Addison 2001; Dewan, *et al.*, 2003; Schonfeld, 2001). The need to diversify the sources of revenue has prompted many online service providers to begin charging customers a subscription or membership fee for the services they use (Olsen 2001; Goldman 2001; Prasad, *et al.*, 2003; Taylor 2001). For online consumers who have grown accustomed to free services, however, the impact of a fee-based service model on their purchasing behavior remains to be seen. Indeed, according to a survey conducted by Greenfield Online (Coupey 2001), 66% of the 3,000 respondents stated that it was the free goods or services that had attracted them to a particular Web site in the first place. Faced with such prevailing attitudes, companies that start to charge for online services may well see their customers "driven away" (Anonymous 2001).

Over the past several years, Internet consumers may have developed certain beliefs and expectations about how online service businesses operate and how readily available they have become. There is a strong belief, for example, that the majority of online service offerings are supported by advertising revenues. Consequently, consumers may expect to continue using these services at virtually no cost to them. Reinforced through repeated online experiences, such beliefs and expectations will be difficult to change (Rust & Lemmon, 2001). Equally plausible, however, is the strong loyalty that certain online service businesses may be able to foster in their customers. The variety and quality of their services offerings may have become so indispensable to their customers that the latter are increasingly willing to pay for such services (Griff & Palmer, 1999; Srinivasan *et al.*, 2002). Without a thorough understanding of such factors that influence consumers' willingness-to-pay, the online service industry's push for a fee-based revenue model is unlikely to be very effective.

Prior studies about fee-based online services have largely focused on electronic libraries, a market in which owners of proprietary information content not available elsewhere can and are expected to charge a premium for access (Anonymous, 2003; Dearie & Fong, 1999; Lawson & Lawson, 2002; McKay, 2000). Several recent studies also examined online music services, where a fee-based model has taken hold, thanks to numerous court challenges mounted by the recording industry against free music download services (Clemons, *et al.*, 2003; Schonfeld, 2001; Walsh, *et al.*, 2003). To providers of other types of online services – notably services such as news, references, electronic mail, travel, etc. – where alternative sources abound and competition is only a few clicks away, overcoming consumers' unwillingness to pay can be a serious challenge. The primary objective of this exploratory study is to identify factors that significantly influence consumer opinions regarding a wide variety of online services that may become fee-based. Specifically, the study investigates the relationship between consumers' willingness to

pay for a given service and a number of plausible causes, including consumers' perceived importance of the online service and their past experience of using that service. In addition, the study explores reasons why consumer may or may not be willing to pay for online services. The findings of the study are expected to contribute to the development of more effective and sustainable revenue-generation models for the online service industry.

### Identifying Factors Influencing Consumer Opinions on Fee-Based Online Services

According to Keeney (1999), e-commerce consumers make purchase decisions based on the net value of the benefits and cost of both the product/service and the *processes* of obtaining it. Indeed, compared to more traditional channels, the online service industry has attracted consumers mainly through adding value to the delivery processes. Technology makes it a simple matter what was unthinkable only a generation ago: unlimited quantities and selections of information and services, from news to travel, from entertainment to match-making, in a variety of media formats, are now accessible around the clock and around the globe. The Internet has made the process of obtaining online services extremely *convenient*. Faced with the economic reality that certain online services may no longer be free, if a consumer believes that the convenience provided by a given service is important, s/he must now decide if such convenience is so important that it is worth paying for. This study therefore explores the possibility that the perceived importance of convenience provided by an online service may have some influence on consumers' willingness to pay for that service.

While Keeney's value proposition assumes that online consumers' behavior results from a rational cost/benefit evaluation, there is now evidence that their past online experience and habit may also play an important role in their future intentions of shopping online. For example, Gefen (2003, also Gefen, *et al.*, 2003) found that consumers' intentions to continue using a given e-commerce vendor are shaped by habit. The more they buy at a website, the more likely they will buy from the same place again. In the context of this study, if a consumer has developed a strong habit of using a certain online service and that service goes from being free to fee-based, it can be argued that s/he would be willing to pay to continue using it. Therefore, a consumer's willingness to pay for an online service ought to be related to how habitual s/he has become in using that service. Consequently, this study further explores the impact of the amount of usage of a specific online service on consumers' willingness to pay for that service.

To a particular consumer, his/her willingness to pay for online services may be further influenced by certain beliefs, expectations, and even value judgments. This study explores a number of these other reasons that might explain why a particular consumer will be willing to pay for online services:

- the consumer might believe that to be fair, one must always pay for the service one gets, be it tangible or intangible;
- the consumer might believe that since online businesses can no longer survive on advertising revenues alone, one must pay to help keep them in business;
- the consumer might expect fee-based services to be quantitatively and qualitatively better than free services and therefore worth paying for (Riggins, 2003; Srinivasan *et al.*, 2002). Likewise, there might also be a number of reasons why a particular consumer will be unwilling to pay, which we must also study:
- accustomed to getting free services in the past, the consumer might find it hard to accept any new charges (Addison 2001; Schonfeld 2001; CNN Headline News 2002);
- the consumer might continue to believe that online service providers could fully rely on advertisement revenues and therefore do not need to charge users;
- the consumer might continue to be concerned about the security of making payments online (Balfour *et al.*, 1998; Yang & Jun, 2002).

Prior research has demonstrated that consumers' demographic characteristics can play important roles in their online purchasing behaviors (Akhter, 2003; Iqbal, *et al.*, 2003; Mowen & Minors, 2001). Due to their differences in age, gender, amount of work experience, etc., consumers may also hold different attitudes and exhibit different behaviors toward such issues as paying for online services. This study therefore also examines the relationship between consumers' demographic characteristics and their willingness to pay for online services.

Finally, earlier studies on online consumer behaviors show that consumers' e-commerce experience, as

measured by their history of making online purchases, may have a particular impact on their perceptions and responses toward issues such as online purchase decision making (Lee 2001) and online privacy and security concerns (Chen *et al.* 2001; Sheehan 2002; Yang & Jun 2002). It is natural to assume that consumers' e-commerce experience would also influence their attitudes and responses toward fee-based online services. Therefore, we also include in this study the amount of e-commerce experience as a potential factor that might influence consumers' willingness to pay.

## RESEARCH METHODS

A questionnaire instrument was developed to collect the following data: consumer attitudes toward fee-based online services, their assessment of the importance of convenience for various online services, their usage of common online services, as well as their opinions on pricing and payment methods. Demographic data such as gender, age group, and number of hours worked were also collected to help explore the relationships between the afore-mentioned attitudes/opinions and the characteristics of online consumers. Finally, the instrument collected data on consumers' e-commerce experience, both in terms of length of that experience (since when the consumer first made an online purchase) and frequency of online purchases (how many online purchases had been made).

A pilot study identified ten most common online services, including email, reference, travel, news, entertainment, health information, weather, sports, auction, and relationship (dating). All of them were listed in the questionnaire. For each of these services, subjects expressed their willingness to pay, their perceived importance of convenience, and their frequency of use (see Appendix for the survey instrument). Responses were measured on a 5-point Likert-type scale. Correlation analyses and *t*-tests were used to analyze the data collected.

The subjects of this study were business students in a large Western state university. Two hundred and thirteen valid responses were collected. Of the 213 subjects, the average age was 25.9, and the average number of hours worked per week was 20.2. 203 subjects reported their gender, with 99 of them being male and 104 being female. This was a gender-balanced sample, with reasonable amount of work and "real-life" experience, and of reasonable maturity.

## RESULTS AND DISCUSSION

### Relationships Between Willingness to Pay, Usage, and Perceived Importance of Convenience

Table 1 presents the average measures of the respondents' willingness to pay, usage, and perceived importance of convenience, broken down by specific online services. Also shown are relative rankings of these measures across the different types of online services.

**Table 1. Subjects' Rating and Ranking on Willingness to Pay for, Usage of, and Importance of Convenience of, Online Services**

<i>Online Service</i>	<i>Willingness to Pay</i>	<i>Rank</i>	<i>Usage</i>	<i>Rank</i>	<i>Importance of Convenience</i>	<i>Rank</i>
Email	3.15	1	4.84	1	4.58	1
Reference	3.03	2	3.03	4	4.06	3
Travel	2.86	3	2.74	5	4.11	2
News	2.52	4	3.65	2	3.95	4
Entertainment	2.49	5	3.14	3	3.75	5
Health info.	2.40	6	2.16	8	3.65	6
Weather	2.10	7	2.56	6	3.59	7
Sports	2.05	8	2.51	7	3.22	8
Auction*	1.86	9	1.59	9	3.14	9
Relationship	1.83	10	1.33	10	2.54	10

\* Users are charged for entering.

(Rating on a 1 to 5 scale, with 5 being the highest)

There appears to be a clear pattern across the three measures. Email, Reference, Travel, News, and Entertainment ranked consistently at the top half as online services that respondents were most willing to pay to use, that they used most often, and that they considered the convenience provided by these services to be the most important. Other services, especially auctioning and relationship (i.e., dating/match-making) services, ranked consistently at the bottom half.

Correlation analyses suggest that the respondents' willingness to pay for a certain online service is related to both their amount of usage and their perceived importance of convenience of that service (among the twenty pairs of correlations, only two pairs are not statistically significant). A closer examination also found a strong relationship between usage and importance of convenience. Significant correlations were observed between usage and importance of convenience for nine out of the ten online services. Therefore, to control for the influences of one factor on the other, partial correlations were conducted and the results are presented in Table 2.

As shown in Table 2, with a majority of the online services, willingness to pay is positively related to either of the two factors: usage and importance of convenience. These results suggest that consumers' usage of an online service appears to influence their willingness to pay for that service, so does their perceived importance of convenience of that service. In other words, unless a consumer is a heavy user of an online service and perceives the convenience provided by that service to be very important, s/he is likely to go elsewhere for services of the same type, if the online service becomes fee-based.

**Table 2. Partial Correlations of Willingness to Pay with Usage of Online Services and with Importance of Convenience of Online Services**

<i>Online Service</i>	<i>Correlation with Usage, controlled for Importance of Convenience</i>	<i>Sig.</i>	<i>Correlation with Importance of Convenience, controlled for Usage</i>	<i>Sig.</i>
Email	.129	.061	.079	.253
Travel	.107	.123	.200	**
Reference	.165	*	.179	**
News	.120	.084	.188	**
Entertainment	.166	*	.173	*
Health info.	.152	*	.271	**
Weather	.153	*	.104	.133
Sports	.274	**	.121	.081
Auction	.206	**	.200	**
Relationship	.260	**	.273	**

\*: significant at 0.05 level

\*\*: significant at 0.01 level

### **Other Reasons for Consumers' Willingness or Unwillingness to Accept Fee-based Services**

In addition to amount of usage and perceived value of convenience, it is plausible that consumers' willingness to pay might be independent of the specific type of services they use. Instead, other reasons could affect their acceptance or rejection of fee-based on-line services. In this study, the respondents were also asked to indicate the extent they agreed/disagreed with a number of other reasons that might explain their willingness/unwillingness to pay. The results of their responses are summarized in Table 3.

An expectation that fee-based online services would be better than free services is the highest rated reason that consumers may be willing to pay. Consumers seem to accept the notion that as long as there is marked differentiation between service qualities, better services are worth more and therefore should be fee-based. On the other hand, it seems difficult for consumers to accept the fact that online services can no longer be supported exclusively by advertising revenues, as it was the lowest rated reason by the respondents. When asked about the reasons why they would not want to pay for online services, the respondents gave the highest rating to the statement,

“The services have been free; why should I pay for them now?” Given the very high rating, it would appear that such a habitual belief is still too strong for online service providers to overcome.

**Table 3. Mean Ratings of Reasons to Pay/Not to Pay for Online Services**

<i>Reasons</i>	<i>Rating</i>	<i>Rank</i>
<b>Willing to pay because</b>		
I would pay for better service	3.34	1
I need the service and want it to survive	3.28	2
it is the right thing to do	3.19	3
advertising revenues are shrinking	2.97	4
<b>Unwilling to pay because</b>		
the services have always been free	4.11	1
they get paid from advertisement	4.00	2
I don't want to use credit card online	3.71	3

(5-point scale, with 5 being Strongly Agree, and 1 Strongly Disagree)

To understand how these opinions might affect consumers' willingness to pay for online services, we conducted correlation analyses of the respondents' overall willingness to pay with the reasons listed above. The results are shown in Table 4.

**Table 4. Correlations of Overall Willingness to Pay with Opinion Items**

<i>Reasons</i>	<i>r</i>	<i>p</i>	<i>Significance</i>
<b>Willing to pay because</b>			
I would pay for better service	0.227	0.012	*
I need the service and want it to survive	-0.027	0.764	N.S.
it is the right thing to do	0.189	0.034	*
advertising revenues are shrinking	0.123	0.177	N.S.
<b>Unwilling to pay because</b>			
the services have always been free	-0.331	0.0001	**
they get paid from advertisement	-0.250	0.001	**
I don't want to use credit card online	-0.046	0.546	N.S.

\*: significant at 0.05 level

\*\*: significant at 0.01 level

Consumers' overall willingness to pay is significantly and positively correlated with the expectation that fee-based services would be better, and with the belief that “pay for what you get” is the right thing to do. Meanwhile, overall unwillingness to pay appears to be significantly impacted by consumers' deeply entrenched “free lunch” habit, and by their perception that online service providers' advertising revenues are sufficient for their financial viability.

**Relationships Between Reasons to Pay/Not to Pay and Consumers' E-commerce Experience**

To measure respondents' e-commerce experience, they were asked to report both the lengths of their online shopping experience (“EC Years” hereafter) and the frequencies of their online purchasing activities (“EC Times” hereafter). We intended to find whether the amount of respondents' e-commerce experience has an effect on their opinions towards fee-based online services. One might postulate that EC Years would very likely be closely related to the EC Times. A correlation coefficient of 0.541 ( $p < 0.01$ ) confirms that this indeed is the case. In order to control for the effects of such correlation between EC Years and EC Times, we calculated partial correlation coefficients between respondents' overall willingness to pay and each of the two variables — EC Years and EC Times, controlling for the other variable, respectively. We found a marginally significant relationship between willingness

to pay and EC Times ( $r = 0.1342$ ,  $p = 0.069$ , controlled for EC Years), but no significant relationship between willingness to pay and EC Years ( $r = -0.0785$ ,  $p = 0.289$ , controlled for EC Times). Partial correlation coefficients were also calculated for reasons why one is willing or unwilling to pay with EC Years and EC Times respectively, controlling for the other variable. Only one reason for not to pay, “don’t want to use credit card online,” is significantly and negatively correlated with EC Times ( $r = -.3732$ ,  $p < 0.01$ ). Overall, it appears that the amount of a consumer’s e-commerce experience does not have a significant impact on his/her willingness to pay for fee-based online services, with the exception that, as a consumer’s e-commerce experience increases, s/he becomes less concerned about the security of making payments online.

### The Differences Between Those Willing to Pay and Those Unwilling to Pay

It would be valuable for e-businesses to identify behavioral differences of those who are willing to pay for online services and those who are not, so they may design their marketing strategies and business models accordingly. To explore such differences, we divided the returned questionnaires into two groups: those who indicated a willingness to pay (the “P” group), and those who indicated an unwillingness to pay (the “NP” group). *T*-tests were then conducted between these two groups with regard to their opinions toward fee-based online services, their willingness to pay for specific online services (such as auction, travel, news, etc), and their demographic characteristics. Only significant results are summarized in Table 5.

**Table 5. *t*-statistics on Differences between the Two Groups: “Pay (P)” and “Not Pay (NP)”**

<i>Items on Which the Groups Are Compared</i>	<i>t</i>	<i>p</i>	<i>Sig.</i>	<i>Mean-NP</i>	<i>Mean-P</i>
“Online services have been free and should remain so”	5.364	0.0001	**	4.55	3.67
“They have advertising revenues”	3.658	0.0001	**	4.31	3.69
Willing to pay for entertainment	-2.485	0.014	*	2.25	2.67
Willing to pay for weather information	-2.073	0.039	*	1.91	2.24
Age	-2.506	0.013	*	2.55	2.93

\*: significant at 0.05 level

\*\*: significant at 0.01 level

As shown in Table 5, the results suggest the following:

- the NP group believes more strongly that since the online services have been free they should stay free;
- the NP group believes more strongly that online services are supported adequately by advertising revenues and therefore do not need to charge consumers;
- the P group is more willing to pay for online entertainments and weather information;
- the NP group is on the average younger than the P group.

### CONCLUSIONS AND LIMITATIONS

The findings of this study have both managerial and research implications. From a managerial perspective, the study suggests that a fee-based online service must be qualitatively better than free services in order to attract paying customers. Further more, in marketing fee-based services, the online industry needs to leverage on consumers’ basic value (of paying for what one gets) to overcome their “free-lunch” mentality. In addition, the industry must continue to educate the public about the fact that advertising revenues alone are not sufficient to keep online services alive. Consumers must be made aware that, unless they are willing to pay for at least part of the cost, many online services they have come to depend on will be unable to survive in the long run.

Our findings further suggest that both perceived importance of convenience and usage may impact consumers’ willingness to pay for *specific type* of online services, such as reference, entertainment, and health information. Given this knowledge, e-businesses may be able to identify more profitable customers and design and execute more effective marketing campaigns. Moreover, it is important to know that “those who will pay tend to pay for certain services,” and that consequently, advertising on the Web sites of those services will be more effective than on the sites of other services. Finally, the study suggests that older consumers may be more willing to use fee-

based online services than younger ones. As a result, the online industry may find it more effective to target fee-based services at older consumers.

From a research perspective, the findings of this study facilitates our understanding of online consumer behavior, specifically factors that may influence consumer attitudes and behavior towards paying for services provided online. Future research could investigate the relationship between consumers' willingness to pay and the types of online services they use. Such knowledge would allow e-businesses to design the best mix of free and fee-based services. Another future direction of research could focus on the effect of different payment models, such as a subscription model or a metered, pay-per-view model. A specific payment model usually has implications on how much a consumer has to pay in order to use a certain amount of service. It is likely that consumers' willingness or unwillingness to pay for online services can be very much a function of the payment model employed.

Caution must be exercised when generalizing the findings of this study. A methodological concern is the student population from which the sample was drawn. Due to geographical and demographical limitations, participants may possess certain attributes that are different from those of the general consumer population in other parts of the country. Future research may need to introduce more diversity in age, education background, work experience, and geographical location into the sample population.

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APPENDIX

SURVEY INSTRUMENT

Scale Item	Question/Statement
Usage	How often do you use each of the online services listed (1 – Never; 2 – Occasionally; 3 – Monthly; 4 – Weekly; 5 – Daily)?
Perceived Convenience	Compared with traditional businesses and media, e-businesses provide convenience to consumers. Convenience means a lot to me. (1 – Strongly Disagree; 3 – Neutral; 5 – Strongly Agree).
Overall Willingness to pay	E-businesses provide convenience, search capabilities, comparison shopping, free reference, etc. Compared with the traditional services (those in a mall, etc.), because of the convenience of obtaining information and service online, (choose one only) a. I am willing to pay more b. I am willing to pay an equal amount c. I am willing to pay less d. I still don't want to pay
Willingness to pay for specific service	To what extent are you willing to pay for each of the online services listed (1 - Least Willing; 3 – Indifferent; 5 - Most Willing)?
Reasons to pay	a. I need the online services; I don't want to see them go out of business. b. I just feel it's the right thing to do: you pay for things you get. c. E-businesses need profits to survive -- but ad dollars are shrinking. d. If they improve their service, they should charge for the better service. (1 – Strongly Disagree; 3 – Neutral; 5 – Strongly Agree)
Reasons NOT to pay	a. The services have been free; why should I pay for them now? b. They already get paid for the ads on their site. c. Just don't want to give my credit card number online. (1 – Strongly Disagree; 3 – Neutral; 5 – Strongly Agree)
Gender	Male/Female
Age	Below 20    20-24    25-29    30-34    35-39    40-44    45+
Work hours per/wk	0-9        10-19        20-29        30+
EC Years	Approximately when did you make your first online purchase (product or service)? 2003 / 2002 / 2001 / 2000 / 1999 / 1998 or earlier
EC Times	Approximately how many times have you made purchases online? 1-5    6-10    11-15    16-20    More than 20 times