



# Ofcom response to BIS consultation on the early implementation of a ban on above cost payment surcharges.

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## Introduction

Ofcom welcomes the opportunity to respond to the Department for Business, Innovation and Skills' ('BIS') consultation on the early implementation of a ban on above cost payment surcharges. As the independent regulator and competition authority for the UK communications industries, we have sought to focus our response on the issues and proposals that are more likely to affect – and, where we are able, provide information relating to - the communications sector.

Ofcom's principal duty under section 3(1) of the Communications Act 2003 is to further the interests of citizens in relation to communications matters and to further the interests of consumers in relevant markets, where appropriate by promoting competition. In carrying out our duties, we need to have regard to the interests of consumers in respect of choice, price, quality of service and value for money (Section 3(5)). We also need to have regard to the needs of elderly and disabled consumers and those on low incomes (Section 3(4)).

Our principal duty is concerned with ensuring that communications markets work well for consumers and for providers that deal fairly with consumers. This means that we seek to ensure that consumers have the information they need to make informed decisions and exercise choice, are not subject to unfair surprises and that inequalities in matters like bargaining power, knowledge and consumer need are not exploited. It also means that providers who act fairly to respond to informed consumer demand should have the opportunity to prosper at the expense of those who do not.

Consumers should know the price they will pay for their communication services and not be taken by surprise by any additional charges they need to pay depending on the payment method they use. In particular, it is important that consumers are not presented with apparently attractive headline prices that are, effectively, subsidised by more obscure ancillary charges for things like the means of payment. Headline prices are more likely to be constrained by competition and can, as a result, be more likely regarded as fair. Ancillary charges are not, or much less so. Consumers and fair dealing businesses should, therefore, be protected by ensuring that charges for goods and services are transparently exposed to the effects of competition. One means of facilitating that is effectively to limit the amounts that may fairly be recovered in ancillary charges to costs directly and specifically related to particular payment methods.

### **Question 1**

**Do you agree that we should implement the ban on above cost surcharges before the EU transposition deadline?**

#### **Comments:**

We agree.

Under the EU Consumer Rights Directive ('CRD'), businesses will be allowed to transparently recover through charges the costs they incur directly related to particular payment methods. For the reasons set out above, we agree that it is important that consumers and fair dealing businesses are protected against excessive payment surcharges.

This is an issue that consumers and consumer organisations have raised complaints and concerns about over a number of years and across a range of sectors including the communication sector. Concerns raised in the communication sector have tended to focus on the additional charges that consumers pay for non-direct debit ('non-DD') payment methods. Consumers on low incomes often choose to pay for their services by non-DD payment methods as they consider this gives them greater control over their expenditure and helps them to manage their budget. Some consumers have no option but to pay by non-DD payment methods where they do not have access to a bank account.

Given concerns about excessive payment surcharges span a number of years and sectors, we think it would be beneficial to consumers to implement a ban on excessive payment surcharges as quickly as possible, ahead of the CRD transposition deadline.

Following agreement of the CRD in October 2011 and the Government's announcement in December 2011, providers will already be familiar with the proposals to ban businesses from imposing excessive payment surcharges on consumers. Providers that do currently apply excessive payment surcharges should already be thinking about the changes they need to make to ensure their charges are fair and reasonable. Early implementation of the CRD will require no action to be taken by, and have little or no adverse impact, on those businesses that already seek to treat their customers fairly and only apply reasonable fees for paying by different payment methods. Indeed, they will benefit from the constraint placed on less scrupulous competitors.

Effective competition delivers choice, better service, lower prices and innovation. In order to benefit from competition, consumers must have confidence that they are able to exercise choice and assert their rights. Consumers who understand the final purchase price they would pay to different providers are more empowered to make better purchasing decisions and this in turn should mean that consumers and fair dealing businesses can enjoy the benefits they should expect from a competitive market.

### **Question 2**

**Do you agree that the exemption for low value, off-premises transactions should not be applied to the payment surcharges provision?**

#### **Comments:**

We agree.

The option for Member States to exempt low value off premises transactions from the provisions in the CRD was intended to avoid administrative burdens being placed on businesses where this was deemed appropriate. There does not appear to be a case for applying the exemption to the payment surcharges provisions.

Rather, a similar logic would apply in respect of these transactions as in respect of any others. We agree that applying the exemption to the payment surcharges provisions could be detrimental to consumers and to those businesses that already seek to deal fairly with their customers with respect to low value transactions. A consistent approach should make it easier for businesses and consumers to understand their obligations and their rights. For all these reasons, it would seem appropriate for contracts of all value to be covered by the legislation on excessive payment surcharges.

**Question 3**

**Do you agree that these sectors should be outside the scope of the payment surcharging provision? Please give reasons and provide evidence if possible.**

**Comments:**

Article 3(3)(m) of the CRD exempts contracts ‘concluded with telecommunications operators through public payphones for their use or concluded for the use of one single connection by telephone, internet or fax established by a consumer’ from the scope of the CRD. At present, Ofcom does not have any specific evidence that would suggest there is a case for applying any of the payment surcharge provisions to these contracts.

**Question 4 (i)**

**To what extent are payment surcharges applied to bookings for package travel? Please provide evidence of the extent and level of surcharging if possible.**

**Comments:**

We are not in a position to answer this question.

**Question 4 (ii)**

**Do you agree that the scope of the payment surcharges regulation should cover package travel sales? If you disagree, please explain your reasoning.**

**Comments:**

We are not in a position to answer this question.

### Question 5

**Do you agree that micro-enterprises should be exempt from any ban on excessive payment surcharges until June 2014? Please provide evidence if possible.**

#### **Comments:**

The vast majority of those regulated by Ofcom are outside the micro-business category. We do not, therefore, have sufficient information or evidence to assist in responding to this question.

### Question 6

**Please state whether in your opinion each of the following potential costs to businesses of accepting payments should, in the case of card payments, be included within the definition of costs borne to the trader. Please give reasons for your answers:**

- a) The merchant service charge**
  
- b) IT, risk management, fraud and operational costs**
  
- c) Fees to intermediaries**
  
- d) Costs to businesses of carrying out intermediary functions internally**
  
- e) Any other potential costs – Please identify**

#### **Comments:**

As noted above, under the CRD businesses will be able to transparently recover in charges the costs directly and specifically related to particular payment methods. Our view is that such charges should, however, be limited to such costs. They should not include the costs of collecting any payment that apply in any event (including in respect of a business's preferred means of payment and/or any in respect of which no surcharge is levied). These are overheads that apply in the ordinary course of business, not costs borne because a particular payment method is used. This approach was reflected in the work we did in our Additional Charges Review<sup>1</sup> in 2008 (and updated in 2010). This related to the application of the Unfair Terms in Consumer Contracts Regulation 1999 ('UTCCRs') to certain terms and charges in contracts for communication services between providers and consumers. These included terms and charges relating to non-DD payment methods.

As part of the review, we issued guidance to try to ensure that providers are aware of, understand and comply with their obligations under the UTCCRs, giving consumers (and, indirectly, fair dealing businesses) appropriate protection from providers using unfair terms. We reviewed and updated our guidance following the Supreme Court judgement in the bank charges case.<sup>2</sup>

In particular, our guidance set out our view that a non-DD charge is likely in many cases to be part of the price the consumer must pay for the package of goods and services they receive under the relevant contract. Provided the contract terms are clear and transparent, we noted the amount of the charge as compared to the goods and services provided in exchange is likely to be an exempt matter and the test of fairness will not apply. Where the relevant term is not expressed in plain, intelligible language and does not meet the transparency requirements, however, we noted that the fairness test will apply to a non-DD charge.

We also set out one way in which we considered the fairness test could apply in relevant cases – this is copied below for ease of reference. In the example we made reference to charges which we

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<sup>1</sup> <http://stakeholders.ofcom.org.uk/consultations/addcharges/?a=0>

<sup>2</sup> <http://stakeholders.ofcom.org.uk/binaries/consultations/addcharges/statement/Guidance.pdf>

considered it could be fair or unfair to collect through a non-DD charge (for the purposes of the UTCCRs). We said we would expect a fair charge to be more likely to reflect only the actual costs incurred by a provider in processing payments made by a particular payment method.

**Excerpt from Ofcom’s unfair terms/additional charges guidance**

*“Non-DD example from Ofcom’s Additional Charges Guidance*

*A consumer who chooses not to pay by DD may cause the provider to incur additional processing costs which are directly attributable to that method of payment. We consider that non-DD terms and charges that are subject to the fairness test are more likely to be considered fair where they seek to recover only these additional costs through the non-DD charge.*

*Such terms are more likely to be unfair if they seek to recover from consumers, as part of the charge, a cost component which does not reflect the providers increased cost of taking payment by a means other than direct debit. For example, a non-DD charge that seeks to recover general ‘bad debt’ costs is less likely fair.*

*In our view there is little evidence of a causal link between a consumer’s choice of method of payment and the risk that the same consumer will fail to pay for the services provided. In particular, it is unclear how and why the choice of method will actually cause the consumer to go into bad debt. The principles applied in this context are consistent with the OFT’s guidance on credit card default payments.*

*We recognise that the method of payment might affect how promptly consumers pay. Consumers who pay by an automated method will only ever pay late when that payment mechanism fails (e.g. due to insufficient funds). However, those who pay by non-DD may pay late due to a number of additional reasons, e.g. they may forget to pay, they may be away on holiday or they may not receive the bill in time due to postal delays.*

*Therefore, in some circumstances it may be fair to recover as part of the non-DD charge costs associated with chasing late payments, such as reminder letters/bills provided these costs are not being recovered by a specific late payment charge. This would be where there is evidence of a clear, causal relationship between payment method and the need to chase late payment.*

*One way we think it may be fair for a provider to calculate and apportion the costs recoverable in a non-DD charge is as follows. The provider could add up the overall annual costs of processing non-DD payments of whatever method. This could then be divided by a reasonable estimate of the total number of consumers it expects would be required to pay the charge, to give the annual costs recoverable from each relevant consumer. These charges can in turn be divided so as to enable their periodic collection.”*

A similar approach would suggest that, in principle, most of the kinds of costs referred to in a – d of Question 6 above should lawfully be recoverable in a payment surcharge limited in accordance with Article 19 of the CRD. One caveat again, however, is that they should only be those costs specifically and directly related to the means of payment (e.g. card payments).

That caveat should preclude the recovery of certain of the costs in b, such as IT and ‘operational costs’ where those would ordinarily be incurred anyway, as overheads in the normal course of business, for the purpose of collecting payment by any means. Those are not costs borne because a particular payment method is used.

That approach in turn raises an interesting question about the position of 'bad debt' costs and the costs associated with chasing late payments. For similar reasons to those outlined above, there does not appear to us any reason why bad debt costs should be recoverable in payment surcharges. We did, by contrast, consider that costs associated with chasing late payments may be recoverable where there is evidence of a clear, causal relationship between the particular payment method used and the need to chase late payment. We question, however, whether the same should apply in the present context.

That is, our previous view concerned the application of the UTCCRs to non-DD contract terms and charges. We assessed how we thought such terms and charges might be assessed for fairness under that legislation. Our starting point was to consider whether a sum would be recoverable in an action for damages for breach of contract, and to use that to consider the charge from an unfair contract terms perspective.

That does not, however, appear to us to be quite the same as considering whether a cost is one "*borne by the trader for the use of*" a means of payment for the purposes of Article 19 of the CRD. There may be a case, therefore, for excluding such late payment costs from the calculation of a lawful payment surcharge. Against that, however, should be weighed the possibility that businesses would still seek to recover these costs, but from all consumers rather than just those who might be more likely to generate them.

We suggest it would be helpful if the guidance BIS is planning to publish alongside the legislation banning excessive surcharges sets out its views on the treatment of 'bad debt' costs and the costs associated with chasing late payments.

### *Social tariffs*

Another point we draw to BIS's attention concerns social tariffs. We suggest it may also be useful to include in any guidance a section on these tariffs.

Social tariffs seek to ensure that consumers on low incomes have access to basic services. In the communication sector, BT has social tariff obligations under its Universal Service Conditions which it discharges through its BT Basic scheme. Kcom also has universal service conditions covering Hull. We note that BT Basic is exempt from any payment processing charge. This helps to ensure that the service is more accessible to consumers on low incomes.

Whilst we note that the new law would impose a maximum limit on payment surcharges, not a default amount, we think the lack of payment processing charges on social tariffs is an important protection for consumers on low incomes. We think that position should be retained following any changes to the legislation on payment surcharges. Government may wish to consider clarifying in the guidance the treatment of payment surcharges in relation to social tariffs.

### **Question 7**

**Please give evidence of the use of payment surcharges for means of payment other than credit, debit, prepaid or charge cards.**

#### **Comments:**

As outlined in response to question 1, individual consumers and consumer organisations have raised complaints and concerns over a number of years about additional charges imposed by communication providers when consumers pay for their services using *any* payment methods other than direct debit. Such charges are applied by most communications providers. Ofcom received over 200 complaints about these charges in each of the last two financial years (263 in 2010-11 and 222 in 2011-12). This is significantly lower than the number of complaints we received about these charges prior to us carrying out the Additional Charges Review (5,846 in 2007-08).

As set out above, Ofcom considered non-DD charges as part of our Additional Charges Review.

### **Question 8**

**Do you agree that ‘costs borne to the trader’ should be an average cost of processing transactions of that type rather than of each individual transaction?**

#### **Comments:**

As noted in response to question 6, we indicated in our guidance on the Additional Charges Review that an average cost approach to determining the relevant cost to be recovered from an individual consumer would be a reasonable approach to take. A cost per individual transaction approach is likely to be overly burdensome on businesses and create uncertainty and confusion for consumers.

### **Question 9**

**Do you have any comments on the draft impact assessment (Annex 3)? In particular we would welcome additional evidence on likely costs and benefits. Any financial data may be provided separately and will be treated in confidence**

#### **Comments:**

We do not hold current evidence that would enable us to comment on this in any detail.

### **Question 10**

**Do you agree that it would be inappropriate having regard to principles of proportionality to impose criminal penalties on traders who breach the payment surcharges provision?**

#### **Comments:**

In our view this is a matter further consideration of which may be appropriate.

We note that the prohibition on excessive payment surcharges would be a clear and certain rule. We note also that Article 19 of the CRD is a maximum harmonisation measure. And, that

- Article 23.1 says, “Member States shall ensure that adequate and effective means exist to ensure compliance with this Directive;” and

- Article 24.1 (headed “Penalties”) says:

“Member States shall lay down the rules on penalties applicable to infringements of the national provisions adopted pursuant to this Directive and shall take all measures necessary to ensure that they are implemented. The penalties provided for must be effective, proportionate and dissuasive.”

This latter provision is in similar terms to the equivalent provisions of the Unfair Commercial Practices Directive, another maximum harmonization Directive, in respect of which criminal penalties apply for breach.

Our view, therefore, is that the adoption of criminal penalties may be appropriate as a means of enforcement of the prohibition on excessive payment surcharges. It is, we suggest, at least a matter worthy of further consideration.

### **Question 11**

**Do you agree with our proposal to grant Part 8 powers to certain enforcers and to complement these powers with a duty to enforce under the specific injunction regime and consumer private remedies?**

### **Comments:**

We agree that, if specific enforcement powers are not given to sectoral regulators directly under the new legislation, it would be appropriate to provide them with enforcement powers under Part 8 of the Enterprise Act 2002. Consumers in regulated sectors bring their consumer law complaints to sectoral regulators and look to them to bring collective enforcement action. That applies across other consumer protection legislation (which is enforceable by sectoral regulators under Part 8, even if not directly under the specific pieces of legislation). Those regulators have expertise in their sectors, enabling them better to take appropriate action.

It would therefore better empower and protect consumers (and fair dealing businesses) to maintain a consistent position (in which sectoral regulators have Part 8 powers across consumer protection law).