

TELEFÓNICA UK LIMITED RESPONSE TO OFCOM CONSULTATION:

PRICE RISES IN FIXED TERM CONTRACTS

(Consultation Published 3 January 2013)

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TELEFÓNICA UK LIMITED RESPONSE: PRICE RISES IN FIXED TERM CONTRACTS CONSULTATION

OUR RESPONSE

Telefonica UK Limited

1. Telefónica UK Limited (“Telefónica”) welcomes the opportunity to respond to Ofcom’s consultation: Price Rises in Fixed Term Contracts¹ (the Consultation).
2. O2 is the commercial brand of Telefonica UK Limited. We are a leading communications company with over 23 million customers².
3. At the beginning of December 2012, we announced a price increase of 3.2% from 28 February 2013 for our pay monthly (PAYM) customers. ✂³. We did not take this decision lightly even though competitors had all announced increases in the preceding 12 months or so.
4. ✂.
5. We had not made this kind of increase before and we knew that, notwithstanding that our mobile phone customers have never had better value⁴, price increases are never welcome. However, we had to make a tough choice and we made clear to our customers why we had made the

¹ <http://stakeholders.ofcom.org.uk/binaries/consultations/gc9/summary/condoc.pdf>

² O2 is the commercial brand of Telefónica UK Limited. We are a leading communications company with over 23 million customers – read more about O2 at www.o2.co.uk/news.

³ The increase of 3.2% applied from 28 February 2013 for pay monthly customers. It excluded Pay As You Go (PAYG) customers, enterprise (corporate) customers, home broadband, mobile broadband and home phone customers. Ofcom does not attribute complaints to a named provider but we would welcome disclosure to us of the number of complaints Ofcom received in respect of Telefónica.

⁴ Ofcom’s research concludes that the cost of a mobile for the average usage level in 2011 has nearly halved over the last six years. Even just last year, to buy a high end smartphone with unlimited minutes, unlimited texts and 1GB of data would cost £67 per month. Today, a customer can buy a high end smartphone (with this tariff value) for under half this cost.

decision: <http://www.o2.co.uk/desktop/prices>⁶: for example, enabling us to continue to invest in services which our customers value (such as Priority Moments and Priority Tickets⁷, access to thousands of free Wi-Fi hotspots across the UK⁸, Guru advice⁹ and cash back if customers recycle their gadgets with O2 Recycle¹⁰). Our customers tell us these services are an integral part of the value we give back to them¹¹.

Treating customers fairly

6. We agree with Ofcom that contract terms should be balanced and fair and that customers should receive the contractual bargain for which they signed up. We believe that being clear and upfront with customers to avoid surprises is important in treating customers fairly¹².
7. We note that Ofcom is concerned that the current law is not working effectively for mobile (and fixed) phone and broadband customers. We agree with Ofcom that it is important that law and regulation effectively addresses the harms it is intended to address and, if the rules are failing to address their objectives, then they should be reviewed.
8. As such, Ofcom's Consultation raises important questions about the right regulatory rules that should be in place (and, in particular, in the communications market, whether they should go beyond that which general consumer protection law requires). We welcome the opportunity to respond to Ofcom's preliminary views. As part of this dialogue we believe that it is important to recognise that UK customers are already benefiting from the

⁶ Notices (either a letter or an email as appropriate) were sent to customers in December 2012.

⁷ <http://www.o2priority.co.uk/About>

⁸ <https://www.o2wifi.co.uk/>

⁹ <http://www.o2.co.uk/guru>

¹⁰ <http://www.o2.co.uk/recycle>

¹¹ For example, our Advent Calendar retail savings offers (within Priority Moments) over Xmas 2012 provided up to £70 savings in total across a variety of retailers.

¹² 

most competitive prices in Europe (and the world) notwithstanding Ofcom's concerns¹³:

- i) This healthy competition means that UK consumers benefit from better mobile phone services at lower prices than most other countries in the world.
- ii) Over the last 5 years, the cost to consumers of using mobile phone services has significantly fallen¹⁴:
 - a. The real cost of owning a mobile phone has nearly halved
 - b. The cost of making a voice call on post pay has reduced by nearly a third.
 - c. In Q1 2012, 49% of new mobile contracts had a monthly rental fee of less than £20. Five years previously this was only 6%.
- iii) The handset subsidy model means that more people than ever before have access to the latest handsets at low (or no) entry level price. Today a customer can buy a high end smartphone from £22 a month (on our new On & On tariff)¹⁵.

9. The overall context here is very important¹⁶.

¹³ Ed Richards, Ofcom CEO: <http://media.ofcom.org.uk/2013/01/23/bidding-in-4g-auction-under-way/>

¹⁴ http://stakeholders.ofcom.org.uk/binaries/research/cmr/cmr12/CMR_UK_2012.pdf)

¹⁵ [https://www.o2.co.uk/shop/phones/samsung/galaxy-s-iii-mini-ceramic-white?cm_mmc=googleuk--brand--Handset%20-%20Samsung%20Galaxy%20S3%20Mini%20-%20O2%20\(Desktop\)-O2%20%20%20Samsung%20Galaxy%20S3%20Mini%20%20%20o2%20%20samsung%20%20galaxy%20%20s%20%20iii%20%20mini%20Broad&gclid=CKKq-sWT_LUCFeXKtAodOX0Acg](https://www.o2.co.uk/shop/phones/samsung/galaxy-s-iii-mini-ceramic-white?cm_mmc=googleuk--brand--Handset%20-%20Samsung%20Galaxy%20S3%20Mini%20-%20O2%20(Desktop)-O2%20%20%20Samsung%20Galaxy%20S3%20Mini%20%20%20o2%20%20samsung%20%20galaxy%20%20s%20%20iii%20%20mini%20Broad&gclid=CKKq-sWT_LUCFeXKtAodOX0Acg)

¹⁶ As the Competition Appeal Tribunal (CAT) explains: “[Ofcom has the] responsibility to gather all relevant facts that they reasonably can before deciding whether or not to impose further regulation on industry. Such a responsibility is also consistent with OFCOM's statutory obligations under section 3(3) of the CA 2003, which requires OFCOM to have regard in all cases to “the principles under which regulatory activities should be transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed”. [§82] CAT Judgement 1094/3/3/08 Vodafone Limited v Office of Communications <http://www.cattribunal.org.uk/238-657/1094-3-3-08-Vodafone-Limited.html>

The law is currently under review

10. Of course, the Law Commission is already undertaking a review of the UTCCRs in respect of how the price and main subject matter exemption should be interpreted following the 2009 Supreme Court decision in *Office of Fair Trading v Abbey National plc.*¹⁷ (and more generally in relation to its 2005 Report¹⁸). Given Ofcom's concerns are with the effectiveness of the current law¹⁹, we are surprised that Ofcom's assessment of the options makes no mention of the Law Commission Review in its Consultation²⁰.
11. Indeed, considering Ofcom's abiding principle is only to intervene where necessary²¹, we are surprised that Ofcom has given no consideration to whether Ofcom's concerns will be addressed via the review of the law. No reference is made to the Review in Ofcom's assessment of the options. We fail to see how Ofcom can have conducted a robust assessment in the absence of such consideration (in particular, in relation to options 1 and 2).

This response

12. As we understand it, since the law allows for the price variation terms in the form Ofcom is concerned about (i.e. price variation terms without an automatic right to terminate without penalty in certain circumstances); Ofcom

¹⁷ http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm

¹⁸ "We have also been asked to review and update our 2005 Report recommendations in relation to our general consumer recommendations. The 2005 Report aimed to bring together unfair terms legislation in one coherent regime, in order to simplify and clarify the law. At that time, our recommendations received strong support from consultees and the Government accepted the Report in principle. We have reviewed our proposals and consider that they remain appropriate. We ask whether consultees still agree with those recommendations." The consultation ran until 25 October 2012. This will be followed by an Advice to the Department for Business Innovation and Skills in spring 2013. Law Commission.

¹⁹ At §2.7 Ofcom explains that the concern with GC9.6 is that "[Ofcom] became aware of issues regarding the interpretation of the term "material detriment" in the part of the condition (GC9.6) relating to CPs obligations to notify subscribers of certain modifications made to the contract and their ability to cancel the contract without penalty."

²⁰ Particularly, since, as the Review notes: "Since the Supreme Court decision, the grey list has assumed much greater prominence than it had before." Ofcom and other enforcement bodies have argued strongly that any term on the grey list, or which resembles a term on the grey list, cannot be within the exemption set out in Regulation 6(2). They are particularly concerned about price escalation clauses, early termination charges and default charges." [§8.45]

²¹ Ofcom's Better Policy Making [§1.1] and Ofcom's Mobile Sector Assessment (2009) [§1.7].

turns to its powers to modify General Conditions (GCs) in order to address the issues it perceives.

13. We recognise Ofcom's desire to respond to the consumer sentiment it sees expressed in its complaints data²² and the Which? "Fixed means Fixed" Campaign. We also understand the importance Ofcom places on its role in protecting consumers. We support Ofcom in its desire to ensure the right regulatory framework is in place.
14. With this in mind we have carefully considered the evidence and the assessment of options Ofcom sets out in the Consultation. We have concluded that there are a number of significant flaws in Ofcom's analysis and that Ofcom's proposed intervention is not the best course of action:
 - i) Ofcom has erred in its analysis (in particular in relation to its complaints data) and proposes a solution which is unlikely to benefit consumers overall because of the likely market implications of the intervention Ofcom proposes²³. We discuss this in our comments below on sections 3 and 4 of the Consultation.
 - ii) Ofcom has failed to justify its intervention against its own Guidelines for Better Regulatory Policy making and the test required of it (in respect of General Conditions) in section 47 of the Communications Act. Moreover, Ofcom's analysis fails to pass the standard of assessment that is required of it by UK appeals bodies (capable of withstanding "profound and rigorous scrutiny")²⁴. We discuss this in our comments below on section 4 of Ofcom's Consultation.

²² Annex 1 for reference.

²³ Which Ofcom fails to assess in a thorough manner.

²⁴ UK appeals bodies currently subject Ofcom decisions to a "profound and rigorous" Scrutiny. *Hutchinson 3G UK Limited v Office of Communications (Mobile Call Termination)* [2008] CAT 11 "*The Tribunal accepts... that it is a specialist court designed to be able to scrutinise the detail of regulatory decisions in a profound and rigorous manner.*"

- iii) Ofcom explains that it is seeking the best outcome for consumers. We do not believe Ofcom's proposals are the best outcome for consumers. We believe Ofcom must rethink its approach:
 - a. In particular, we believe that if any regulatory intervention is justified, Ofcom's Option 2, addressing greater transparency, is the most appropriate. Ofcom already has General Condition 23 to readily assist in addressing the issue of surprise (if indeed any remains given the widespread publicity and experience of the issue in the pay monthly base of operators)²⁵.
 - b. Were Ofcom to proceed with its Option 4, we do not support the way in which Ofcom proposes to deal with the range of costs which are outside of our control – we believe these elements must be removed were Ofcom to continue with Option 4.
 - c. We also believe Ofcom must give careful consideration to the scope of the prices it seeks to regulate with this intervention, in particular its proposals beyond subscription prices.
- 15. We explain why we believe Ofcom should reconsider its assessment. And why we propose an alternative conclusion to that which Ofcom has reached. We discuss this in our comments below on section 5 of the Consultation.
- 16. For ease of reference, we have structured our response using the section headings as they appear in the Consultation. We seek to deal with the points Ofcom raises as they arise in each section of the Consultation. This results in some repetition of points but this is consistent with the flow of the Consultation itself.

²⁵ Ofcom recognises that the case for adopting a transparency measure would be strong if there was some ambiguity about whether price rises in fixed terms contracts can create countervailing benefits for customers. By Ofcom's own assessment, they do, although Ofcom argues they are small. We disagree, we consider that the flexibility afforded by the current law allows wider benefits – and our customers value this - and as such option 2 should not be readily discounted.

SUMMARY (Section 1)

Ofcom's analysis

17. In summary, Ofcom concludes that the volume and nature of consumer complaints to Ofcom as well as the Which? campaign demonstrates sufficient evidence that current consumer protection rules are not working.²⁶ Since the general law (primarily UTCCRs) does not prohibit price variation terms (provided they meet certain criteria), Ofcom considers a range of sector specific options, but concludes amending GC 9.6 is the appropriate response²⁷²⁸.

Consumer Protection Rules

18. We believe it is important that law and regulation effectively addresses the harms it is intended to address and, if the rules are failing to address their objectives, then they should be reviewed²⁹.
19. Ofcom points to its complaints postbag and the Which? survey to evidence that the current rules are failing customers. Whilst consumer sentiment as expressed in complaints and surveys is an important factor to consider, Ofcom must consider all relevant evidence and context as part of its policy making³⁰. We believe Ofcom's assessment of the complaints data is not sufficient to withstand the profound and rigorous analysis demanded³¹ and

²⁶ Ofcom explains at §1.2 that it is concerned with the effectiveness of the current rules: i) General Condition 9.6, and ii) the Unfair Terms in Consumer Contracts Regulations (the UTCCRs). Ofcom's concerns arise because of: the level of complaints made to Ofcom (see Annex 1), and the number of signatories who have signed up to Which? Campaign. <http://www.which.co.uk/campaigns/technology/fixed-means-fixed/pledge-your-support/>

²⁷ After considering four possible solutions, Ofcom's preference is to change the General Condition 9.6, to enable customers to terminate their fixed term contracts without penalty should prices increase during the term of the contract. This is notwithstanding that, as Ofcom itself recognises, the law (UTCCRs) explicitly allow such price increases in certain circumstances.

²⁸ Given that Ofcom has concluded the law must be changed, that must mean Ofcom has concluded that the price rises about which it has received complaints are lawful, or of insufficient harm, to justify enforcement action.

²⁹ However, Ofcom must be careful not to conflate expressions of dissatisfaction with consumer detriment. That one is expressed, does not mean the other necessarily follows.

³⁰ As both its Better Policy Making Principles and the Competition Appeals Tribunal require.

³¹ CAT Judgement 1094/3/3/08 Vodafone Limited v Office of Communications <http://www.cattribunal.org.uk/238-657/1094-3-3-08-Vodafone-Limited.html>

does not justify the sector specific intervention Ofcom proposes. An objective analysis of the volume and nature of complaints made to Ofcom does not support Ofcom's conclusions.

Ofcom proposes a significant intervention in a competitive market – beyond that which consumer law provides

20. Ofcom proposes a significant intervention in the communications market.
21. It is important that any such interventions are carefully thought through with a rigorous assessment of their impact and consequences. As Ofcom's "Better Policy Making" [§1.1] emphasises³²:

"The option of not intervening...should always be seriously considered. Sometimes the fact that a market is working imperfectly is used to justify taking action. But no market ever works perfectly, while the effects of...regulation and its unintended consequences, may be worse than the effects of the imperfect market"

Better Regulation Task Force (September 2003)

22. This principle is also emphasised by the Competition Appeals Tribunal (CAT):

"The principle of proportionality requires that any action by OFCOM shall not go beyond what is appropriate and reasonably necessary to achieve their stated objectives. Also, where a choice exists between equally effective measures that might be adopted to address a problem, recourse should be had to the least onerous measure that will achieve the stated aims. The requirement that OFCOM have regard to the principle of proportionality in performing their duties is set out in section 3(3) (a) of the CA 2003." [51]³³

³² <http://stakeholders.ofcom.org.uk/consultations/better-policy-making/>

³³ *ibid*

23. Ofcom's proposed intervention goes beyond the balance struck by current consumer protection law and required by the Universal Services Directive (USD)³⁴. Furthermore, it goes beyond the balance the Law Commission proposes to retain in its Review of the law in this field (the Commission proposes retaining the 'Grey List').
24. That Ofcom proposes to implement a significant sector specific intervention which is inconsistent with OFT's Guidelines and without even considering the Law Commission's recommendations in respect of the 'Grey List' is unsound.

Ofcom's proposed intervention fails to satisfy Section 47 (2) of the Communications Act - Ofcom has erred in its assessment and needs to rethink its proposals

25. As we discuss in this response, Ofcom has erred in its analysis and proposes a solution which is unlikely to benefit consumers in the manner Ofcom intends. As Ofcom itself recognises, the logical result of its intervention is that the increaseses in costs currently addressed via price variation clauses will simply be dealt with elsewhere – for example, in tariff restructuring, handset subsidies, general risk premium or some other outcome³⁵.
26. We believe, Ofcom's intervention fails in its regard to:
- i) Ofcom's Better Policy Making principles,
 - ii) Section [47] of the Communications Act,
 - iii) Withstanding the "profound and rigorous scrutiny" test required by the CAT³⁶.

³⁴ Universal Services Directive (USD) (2009/136EC which amended Directive 2002/22/EC

³⁵ See §6.40 and §6.41 of the Consultation.

³⁶ *ibid*

27. Ofcom cannot safely proceed on this basis.

The UK mobile market is effectively competitive and UK customers benefit from the lowest prices in Europe

28. In its 2009 Mobile Sector Assessment, Ofcom reaffirmed that the mobile market was effectively competitive and concluded that:

“Specifically, our bias against intervention and our wider telecommunications strategy lead us to continue to prefer to maintain healthy, infrastructure-based competition at the deepest level possible to produce differentiation in mobile services and pricing.” Where intervention was necessary, transparency/ access to information was the preferred approach³⁷.

29. Against this deregulatory backdrop, the UK market has delivered the lowest prices in Europe.³⁸
30. We are concerned at the robustness of the impact analysis Ofcom undertakes in its Consultation. In particular, Ofcom fails to consider the wider outcomes for consumers under the current regulatory regime. It cannot therefore have robustly considered if its intervention will achieve an overall better outcome for consumers. This is a considerable flaw in its regulatory policy making in this matter.

Ofcom’s Complaints Data

31. We have given careful consideration to the complaints data Ofcom provides (copy included in Annex).

³⁷ *“There are areas where we need to be prepared to intervene if the market does not deliver **good outcomes for citizens and consumers**. Our current priorities are to ensure: easy and reliable switching; **access to information to allow consumers to get a good deal**; effective complaints and dispute handling for new market entrants; protection for consumers from misleading or exploitative practices; and ensuring that vulnerable consumers are not disadvantaged”*. [§1.7] [Emphasis added].

³⁸ *ibid*

32. In our view, neither the volume nor the nature of the complaints justifies Ofcom's intervention in the manner Ofcom maintains. For example, some 80% of the volume of complaints relate to one provider³⁹. We believe that Ofcom's assessment would not meet the test required:

"The essential question for the Tribunal is whether OFCOM equipped itself with a sufficiently cogent and accurate set of inputs to enable it to perform a reliable and soundly based CBA".[47]⁴⁰

33. If Ofcom is to interpret complaints as a barometer of consumer expectation (and we do not accept the data can be relied upon in this respect because of its inherent bias), then the most Ofcom can argue is that it is a barometer in respect of those customers of that one provider and that one provider's terms (or explanation thereof). It is not robust "volume" evidence of systemic issues. We discuss this in our comments on section 4 and 5 of Ofcom's Consultation.

Ofcom's assessment of the Options

34. Ofcom explains that it is seeking the best outcome for consumers. We do not believe Ofcom's proposals are the best outcome for consumers since, as Ofcom recognises, the logic of its intervention is that tariffs may be restructured, for example, with risk premiums baked into all tariffs and handset subsidies reduced⁴¹. We believe Ofcom must rethink its approach.
35. We discuss this in our comments on section 5 of the Consultation.

Ofcom's role in respect of the UTCCRs

36. Ofcom's Enforcement Guidelines⁴² explain:

³⁹ Ofcom explains that most complaints were in respect of mobile, however, Ofcom is not explicit that this relates to a mobile provider. Ofcom provides no estimate of the proportion of the PAYM base which the complaints represent, in particular, when the 80% relating to one provider is removed.

⁴⁰ Competition Appeal Tribunal. Ibid.

⁴¹ We note these aspects are not made clear in Which?'s 'Fixed means Fixed' "pledge" pages.

⁴² http://stakeholders.ofcom.org.uk/binaries/consultations/draft-enforcement-guidelines/annexes/Enforcement_guidelines.pdf

“Ofcom also has the power to enforce the UTCCRs directly (as a “Qualifying Body” under the UTCCRs), rather than under the provisions of Part 8 of the Enterprise Act. Ofcom will generally consider complaints about potentially unfair terms in standard consumer contracts under the UTCCRs directly. Ofcom may consider not only the terms complained about, but also the other terms and conditions of the contract in question where we consider this is appropriate in order to prevent consumer harm.” [§2.27] [Emphasis added]

37. Ofcom’s Guidelines then explain how it will enforce the UTCCRs.
38. However, Ofcom does not make clear in the Consultation whether it has followed its Enforcement Guidelines. Ofcom does not explain whether it has considered action in respect of the 1644 complaints under the UTCCRs directly. So either Ofcom has not acted in accordance with its Guidelines, or it has concluded that there is no case to answer under the UTCCRs or it has concluded that because of administrative priority it will not take action (whether this is a function of the “complexity” and uncertainty Ofcom perceives in the UTCCRs or not).
39. As we explain elsewhere, if the conclusion is that the UTCCRs are themselves “faulty” then the right course of action is to consider the UTCCRs under the Law Commission Review – not under sector specific regulation. And as we explain elsewhere, the Law Commission has indeed proposed measures to make clear that price variation/ escalation terms can be fair depending on circumstance. The “uncertainty” Ofcom perceives in the UTCCRs is being addressed. Unfortunately, the sector specific intervention Ofcom proposes is inconsistent with the course of action proposed by the Law Commission. In a communications marketplace where consumers will purchase bundles of services – some regulated under General Conditions, some regulated under the UTCCRs, this inconsistency of rules is unhelpful for consumers, providers and regulators alike. Ofcom is creating inconsistency, not solving uncertainty.

The most balanced solution for our customers

40. Ofcom explains that it is seeking the best outcome for consumers. We do not believe Ofcom's proposal is overall the best outcome for consumers and we believe Ofcom must rethink its approach.
41. We believe that if intervention is justified (following a robust evidence based assessment), the most balanced and appropriate solution is Ofcom's option 2, the promotion of greater transparency. Ofcom has the tools in place to do this (General Condition 23 and enforcement powers in respect of the UTCCRs). We are not convinced that action under option 2 in relation to clarity with customers would take "some time to develop" as Ofcom fears [6.58]. Indeed, the ASA has already ruled in respect of advertising⁴³.

Premature for Ofcom to intervene given the Law Commission review⁴⁴⁵

42. The Law Commission is already undertaking a review of the UTCCRs in respect of how the price and main subject matter exemption should be interpreted following the 2009 Supreme Court decision in Office of Fair Trading v Abbey National plc.⁴⁶ and more generally in relation to its 2005 Report⁴⁷. We discuss this further in the response but given Ofcom's concerns

⁴³ http://www.asa.org.uk/Rulings/Adjudications/2013/2/Vodafone-Ltd/SHP_ADJ_210326.aspx

⁴⁴ http://lawcommission.justice.gov.uk/consultations/unfair_consumer_contracts.htm

⁴⁵ http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm

⁴⁶ http://lawcommission.justice.gov.uk/areas/unfair_terms_in_contracts.htm

⁴⁷ "We have also been asked to review and update our 2005 Report recommendations in relation to our general consumer recommendations. The 2005 Report aimed to bring together unfair terms legislation in one coherent regime, in order to simplify and clarify the law. At that time, our recommendations received strong support from consultees and the Government accepted the Report in principle. We have reviewed our proposals and consider that they remain appropriate. We ask whether consultees still agree with those recommendations." The consultation ran until 25 October 2012. This will be followed by an Advice to the Department for Business Innovation and Skills in spring 2013. Law Commission.

are with the effectiveness of the current law⁴⁸, we are surprised that Ofcom makes no mention of the Law Commission Review in its Consultation⁴⁹.

43. The Law Commission Review explains: *“the Department for Business, Innovation and Skills (BIS) is consulting on a package of measures to clarify consumer law, to be introduced by both primary and secondary legislation. The aim is to put a Bill to the UK Parliament in the 2013 to 2014 Parliamentary session. This provides an opportunity to clarify the law on unfair terms as it affects consumers.”* [§1.3]. The Law Commission recommends making clear:

“We agree that a price escalation clause cannot be within the [price] exemption. The CJEU has been explicit on this point. In Nemzeti, it stated that the “exclusion cannot apply to a term relating to a mechanism for amending the prices of the services provided to the customer. We think that it is important to recognise this explicitly in the legislation.” [§8.46]

44. Given Ofcom’s abiding principle is only to intervene where necessary, we are surprised that Ofcom has given no consideration to whether Ofcom’s concerns will be addressed via the review of the law. We believe that option should properly be considered. It has not and we fail to see how Ofcom can have conducted a robust assessment in the absence of such consideration.

Our detailed response

45. We are concerned that Ofcom’s analysis fails in regards to the Competition Appeal Tribunal’s clear expectation:

⁴⁸ At §2.7 Ofcom explains that the concern with GC9.6 is that “[Ofcom] became aware of issues regarding the interpretation of the term “ material detriment” in the part of the condition (GC9.6) relating to CPs obligations to notify subscribers of certain modifications made to the contract and their ability to cancel the contract without penalty.”

⁴⁹ Particularly, since, as the Review notes: *“Since the Supreme Court decision, the grey list has assumed much greater prominence than it had before. Ofcom and other enforcement bodies have argued strongly that any term on the grey list, or which resembles a term on the grey list, cannot be within the exemption set out in Regulation 6(2). They are particularly concerned about price escalation clauses, early termination charges and default charges.”* [§8.45]

“It is the duty of a responsible regulator to ensure that the important decisions it takes, with potentially wide ranging impact on industry, should be sufficiently convincing to withstand industry, public and judicial scrutiny.” [§47]⁵⁰

46. We discuss these comments in greater detail in the remainder of this response.

⁵⁰ *ibid.*

INTRODUCTION (Section 2)

Ofcom's roles in protecting consumers

47. In this section, Ofcom sets out its objectives and duties in relation to consumers.
48. Ofcom explains the volume of customer complaints it has received has caused it to re-assess the views it held when it transposed Article 20(2) of the Universal Services Directive.
49. Ofcom notes that the average length of new mobile contracts has increased in recent years and that *“these longer minimum term contract periods may be a factor influencing consumer concerns.”*
50. We believe that the context Ofcom provides is important. Yet in referring to the evolution of longer term contracts Ofcom fails to provide the full context, including:
- i) The UK mobile market is effectively competitive and UK customers benefit from the most price competitive mobile phone market in Europe and better services at lower prices than most other countries in the world.
 - ii) The increasing length of contracts is associated with the growth in smartphones (and the associated subsidy required to bring those to market).
 - iii) That customers have the choice of PAYM with heavily subsidised handsets or PAYG without such heavy subsidies or indeed SIM only. Consumers are choosing PAYM.
51. As we explain elsewhere, it is very important Ofcom provides the full context in its assessment – this is emphasised by the Competition Appeal Tribunal.

52. We comment on Ofcom's assessment of the complaints and more generally on the General Impact Assessment Ofcom explains its Consultation represents⁵¹ (see our comments on section 4 and 5 of the Consultation).

The UK mobile market is effectively competitive and UK customers benefit from better services at lower prices than most other countries in the world

53. We are surprised that, in concluding that the current rules are ineffective in protecting customers, Ofcom fails to recognise that under the existing rules the metrics for UK consumer benefit are positive:

"The UK is the most price competitive mobile phone market in Europe¹. Healthy competition means that UK consumers benefit from better services at lower prices than most other countries in the world."⁵²

54. This is not consistent with the scenario Ofcom speculates is emerging: a market in which unfair contract terms lock consumers into a spiral of price increases – leaving them with no choice but to stick with their provider. §4.16.

Ofcom assessment of the outcomes

55. Ofcom's assessment considers a variety of customer outcomes to its intervention. The type of response EE has recently announced ("Fix your Tariff" offer⁵³) is one such response Ofcom generically considered. As Ofcom will note, this charges a premium of between 50p and £2 per month depending on tariff. Ofcom judges that these outcomes are acceptable. However, Ofcom has not cited any consumer research which demonstrates these outcomes are preferable to the current position. It simply cites

⁵¹ Compare for example the detail of the Impact Assessment Ofcom made in respect of the introduction of General Condition 23 to that which it makes in the Consultation. See Annex 2 Assessment of consumer harm and the costs and benefits of our preferred option of <http://stakeholders.ofcom.org.uk/binaries/consultations/mobmisselling/statement/statement.pdf>

⁵² Ed Richards, Ofcom. <http://media.ofcom.org.uk/2013/01/23/bidding-in-4g-auction-under-way/>
⁵³ <http://www.guardian.co.uk/money/2013/mar/01/orange-t-mobile-price-increase>

complaints data and presumes that consumers will prefer any alternative. That is not a robust assessment of the options.

56. Ofcom fails to adequately consider whether the significant step of intervening in a market which is already delivering better services at lower prices than most of the world outweighs the potential of counter productive outcomes.

Ofcom Duties

57. Ofcom explains that it must be prepared to intervene if “*things aren’t working as they should*” [§2.5]. We agree, Ofcom must be prepared to intervene where the case is clear that intervention is required (taking into account Ofcom’s bias against intervention). However, we do not believe that Ofcom has made the case for the intervention it proposes. Ofcom is required to do so under Section 47 (2) of the Communications Act.

58. We discuss this further in the Legal Framework section of this response.

General Condition 9: monitoring and enforcement programme

59. Ofcom explains that the purpose of its programme was “*to monitor compliance [with General Condition 9] following changes made to GC9 to implement the revised EU electronic communications framework in May 2011 ETC.....*” [§2.6]
60. Ofcom explains that it became aware of “*issues regarding the interpretation of material detriment*” in GC 9.6.[§2.7]. We note Ofcom refers to issues of interpretation rather than non-compliance.
61. Ofcom also remarks that it also noted a “*significant increase in complaints to our Consumer Contact Team from consumers affected by price rises*”. [§2.8]
62. It is not clear if Ofcom is suggesting a causal link between its transposition of the USD (and the retention of the “material detriment” test). If it were, then we

would point out that (as Ofcom itself explains) the material detriment test had already been present in GC9 for some years (as at 2011's review).

63. Ofcom explains that it fears that without action, there will be a continued cycle of price variation clauses. Ofcom's approach does not avoid that. Clearly, if underlying costs are increasing then these will need to be recovered – as Ofcom recognises, for example, by baking in the risk premium into headline (or other) prices or some other outcome.
64. Ofcom's action is not preventing costs being recovered through pricing. It is simply replacing the possibility of fair price variation clauses being exercised in the future with the likelihood that risk premiums will be reflected in prices going forward (or other tariff restructuring measures).
65. Ofcom explains that the trigger for this consultation has been the volume and nature of complaints. We discuss Ofcom's analysis in detail in our comments below on sections 4 and 5 of the Consultation.

Ofcom's General Impact Assessment

Ofcom's proposal

66. Ofcom has concluded that: *"consumers need additional protection from price rises in fixed term contracts ..."*⁵⁴
67. Ofcom concludes that existing rules⁵⁵ are ineffective and not achieving the *"basic aims of fairness"* which Ofcom asserts at §1.4 and §1.5, being (presumably) Ofcom's interpretation of the law (UTCCRs). We discuss the relationship with UTCCRs later in this response. Ofcom also says that GC9.6 *"seeks to give consumers similar protection"* (but elsewhere explains GC 9 and UTCCRs are separate).

⁵⁴ We note Ofcom's reference to Consumers. Ofcom previously made clear that GC9.6 applied to Business customers as well as Consumer.

⁵⁵ Which, as Ofcom recognises, in respect of GC 9.6 were introduced in Ofcom's Statement (following consultation) of 23 May 2011.

68. Ofcom then says: *“Ofcom’s view is that there can be no reasonable objection to rules that seek to achieve these aims of fairness but on its assessment the current rules are not achieving Ofcom’s interpretation of fairness and hence there needs to be “additional rules”.*
69. Ofcom suggests that no reasonable objection can be raised to its proposals.
70. Whilst Ofcom may believe there can be no reasonable objection, this does not mean that the robustness of Ofcom’s analysis should be any less. Ofcom’s proposals for sector specific intervention must still meet its Better Regulation Principles and the tests demanded by Section 47 of the Communications Act and the Competition Appeal Tribunal.

Furthering the interests of consumers - Ofcom’s duties

71. Ofcom explains that:
- “Under section 3(1) of the Communications Act 2003, Ofcom’s principle duty 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.” [§2.1]*
72. And that, in performing its duties under section 3(1):
- “Ofcom must have regard, in all cases, to the principles under which regulatory activities should be transparent, accountable, and proportionate. consistent and targeted only at cases in which action is needed, and to any other principles appearing to us to represent the best regulatory practiceSection 3(5), meanwhile, says that in performing our duty of furthering the interests of consumers, Ofcom must have regard, in particular, to the interests of those consumers in respect of matters including price.” [§2.2].*

73. Ofcom fails to adequately consider whether the significant step of intervening in a market which is already delivering better services at lower prices than most of the world outweighs the potential of counter productive effects, including in respect of price.
74. Ofcom also explains that it is under a duty to act in accordance with the six Community Requirements:

“The six Community Requirements give effect, amongst other things, to the requirements of Article 8 of the Framework Directive (2009/140/EC which amended Directive 2002/21/EC). These include, in particular, the requirement to promote competition in relation to the provision of electronic communications networks and services by ensuring that users derive maximum benefit in terms of choice, price and quality (Art 8(2)(a)), and the requirement to promote the interests of citizens by ensuring a high level of protection for consumers in their dealings with suppliers (Art 8(2)(b)) and by promoting the provision of clear information, in particular requiring transparency of tariffs and conditions for using publicly available electronic communications services (Art 8(2)(d)).” [§2.4] [Emphasis added]

75. Whilst we recognise that promoting the interests of consumers includes *“ensuring a high level of protection for consumers in their dealings with suppliers (Art 8 (2) (b), we would also point out 8 (2) (b) continues “in particular by ensuring the availability of simple and inexpensive dispute resolution procedures carried out by a body that is independent of the parties involved”* and, furthermore, as we highlight above, it makes clear that promoting transparency is an important element.
76. As we discuss below, Ofcom concludes that *“given the risks of greater intervention in the market, the case for adopting a transparency remedy would be strong if there were some ambiguity about whether price rises in fixed term contracts can create countervailing benefits for the consumer.”* [6.22]. However, we reach a different conclusion in relation to Ofcom’s

assessment that “...there are few, if any, corresponding benefits to consumers from contract terms providing for price increases.” [6.22]. We discuss this in more detail in our comments on section 5 of the Consultation. We believe that were regulatory intervention to be necessary, option 2 is more consistent with the exercise of Ofcom’s duties than the solution it proposes (option 4).

77. Ofcom makes clear it “wants to make sure that consumers get the best choice and value for money from their communications services and are protected from unfair terms and practices, while allowing competition to thrive. We need to be prepared to intervene if things aren’t working as they should”.
78. We support this intent. However, as Ofcom recognises, any intervention should be as a last resort and moreover, must be objective, transparent, proportionate and non-discriminatory. We believe Ofcom’s proposal does not meet these requirements in all respects and that a more balanced solution given Ofcom’s duties would be Option 1 in light of the Law Commission’s review or, where intervention is justified by robust evidence, Option 2.

Do the benefits of Ofcom’s proposal outweigh any disadvantages for customers?

79. In section 6 of the consultation, Ofcom considers whether the disadvantages arising from its proposed changes (in particular in relation to subsidised handsets) would be outweighed by the protection offered by option 4. Ofcom concludes the “protection” of its proposals outweighs the disadvantages [§6.42].
80. Ofcom simply says it considers providers will continue to have strong incentives to offer customers competitive and attractive deals for handsets. No doubt competitive incentives will remain. However, that is not the same as assessing whether the outcome from Ofcom’s intervention makes things better overall for customers. As we discuss below, there are a range of market responses which may arise, including:

- i) Ofcom notes that some re-structuring of tariffs might arise. Whilst there is likely to be a number of ways in which providers may respond, Ofcom must recognise the risk that cost increases are likely to be borne by customers in some form (whether in price, quality, choice or value etc).
 - ii) Communications Providers may “bake” the risk premium into prices at the outset. Prices will thus reflect the risk automatically and consumers bear that risk automatically. Ofcom’s judgement appears to be that consumers prefer to pay the risk premium for certain (e.g. as would be the case were it to be “baked in” to headline prices), rather than contract on the possibility that a price increase might arise. Further, Ofcom is, in effect, removing consumers choice in the matter by its proposed change to GC9.6.
 - iii) Price changes might come in “greater” steps depending on the degree to which risk premiums are baked in – increasing the differential between old and new tariffs⁵⁶.
81. Ofcom is determining that consumers would prefer the certainty of a higher headline price (with the risk premium) compared to the possibility of a price variation in the future. Ofcom cites no evidence to support that this is a better deal for customers than the current position. For example in respect of handsets, Ofcom makes no attempt to quantify the amount the various price increases it cites in Annex 7 have added to consumers bills vs the amount of handset subsidy consumers receive.
82. As Ofcom notes, “*The UK is the most price competitive mobile phone market in Europe*”⁵⁷. That Ofcom makes no mention of this or indeed the Law Commission’s own review of the UTCCRs emphasises the narrowness – and hence flaws – in Ofcom’s impact assessment.

⁵⁶ And the complexity and cost of ring-fencing changes between existing and new tariffs and contracts will increase. The system challenges of the proposed solution will require assessment.

⁵⁷ Ed Richards, Ofcom, *ibid*

Ofcom's Consultation process

83. We welcome the opportunity to respond to Ofcom's consultation. We do not believe Ofcom's assessment and proposed intervention meets the standards required of Ofcom's Better Policy Making principles, section 47 of the Communications Act and the "profound and rigorous scrutiny" required of the Competition Appeal Tribunal⁵⁸.
84. In the next sections of this response we discuss Ofcom's assessment of the Legal Framework, the Consumer Harm and other issues and the options considered.

⁵⁸ibid.

LEGAL FRAMEWORK (Section 3)**Introduction**

85. In this section, we comment on Ofcom's powers in relation to setting/modifying General Condition 9.6 and consumer protection law more generally.

86. We explain why we believe Ofcom's proposal to amend GC 9.6 fails to meet the test required in Section 47 (2) of the Act.

General Condition 9*The provenance for GC 9.6*

87. Ofcom explains that:

"GC9.6 is included pursuant to section 51 (1) (a) of the Act and is intended to give effect to Article 20 (2) of the Universal Services Directive (USD) (2009/136EC which amended Directive 2002/22/EC) ..." [§3.6]

88. And at §3.7 and §3.8 Ofcom explains that:

- i) In 2003, Oftel⁵⁹ read into the then Article 20(4) of the USD the test of "material detriment". This reflected the test the OFT used in respect of the UTCCRs to determine whether contractual terms were fair or not;
- ii) In 2011, Ofcom retained the material detriment test because it considered it was still relevant and reflected consumer protection rules:

"Ofcom considers that such a threshold is still relevant and likely generally to reflect current consumer protection in this

⁵⁹ Ofcom's predecessor

area³⁷. That is, under the UTCCRs contract terms are unfair if, amongst other things, they create a “significant imbalance” in the consumer’s (subscriber’s) and supplier’s (CP’s) rights and obligations under the contract. Contract terms which could allow a supplier to change the contract in a significant way could well unbalance the contract and are under strong suspicion of unfairness. This is reflected in the provisions of paragraphs 1 (j), (k) and (l) of Schedule 2 of the UTCCRs, which say that various terms providing for contractual variation may be unfair. Retaining a “material detriment” requirement would therefore generally reflect the “significant imbalance” requirement used to determine the unfairness of relevant contract terms³⁸

- iii) Ofcom explains at §3.9, that it considered that its approach (the retention of the material detriment test) was “in line with the requirement for Framework obligations to be exercised in a proportionate manner, whereby, in this case, any proposed contract modifications must materially affect the subscriber before that subscriber can choose to exit from the contract.”
- iv) And in 2011⁶⁰, Ofcom explained that its implementation of GC9.6 was thus objectively justifiable because:

“the amended requirements directly reflect the requirements set out in Articles 20, 30(5) and 30(6) of the revised USD, which Ofcom is obliged to implement,” [§7.32]

- 89. Ofcom concluded the material detriment test remained consistent with the requirement for Framework obligations to be exercised in a proportionate manner [§3.9].

⁶⁰ <http://stakeholders.ofcom.org.uk/binaries/consultations/gc-usdc/summary/gc-usdc.pdf>

90. Accordingly, between 2003 and 2011, Ofcom and its predecessor considered that the retention of the material detriment test was objectively justified and proportionate in relation to the UTCCRs and the express requirements of the Universal Services Directive. Now, in 2013, Ofcom argues that the removal of the very same test is also consistent with the the “express requirements” of the Directive.
91. It is clear that as recently as 2011, Ofcom considered that it had implemented the relevant Articles of the USD correctly via GC9.6. Accordingly, it is not necessary to make the proposed amendment to properly implement the Directive.
92. Ofcom cannot have it both ways. It cannot argue that it is required to make the change proposed in order to implement the “express requirements” of the Directive, since it has already made clear (in 2011) that the current GC9 properly implements the USD. Ofcom must act consistently.
93. Ofcom cannot take lightly revisiting the established regulatory assessment of 2003 to 2011. We appreciate that Ofcom remarks that in light of the level of customer complaints and Which? Campaign it has “*re-assessed the views we took when transposing the requirements of Article 20(2) of the Universal Services Directive*” (and we discuss the evidence Ofcom puts forward elsewhere). However, Ofcom sets a dangerous precedent. To revisit established regulatory decisions previously judged to be objective, proportionate, transparant and non-discriminatory and reverse them (which is what Ofcom is doing by removing material detriment in respect of price variations) is to introduce uncertainty into the regulatory regime and the market. For example, does this mean that Ofcom will revisit every transposition decision it has taken in light of customer complaints and seek to change it? Is Ofcom suggesting that in retaining the “material detriment” element in 2011 it did not consider that those terms might be relied upon?

94. Ofcom has a duty to act consistently. We see a clear lack of consistency here in respect of Ofcom's assessment of the requirements of the USD.⁶¹

Are the terms which Ofcom is concerned about "modifications" pursuant to the Framework?

95. We note Ofcom gives no consideration to whether, the price variation terms about which it is concerned result in "modifications to the contractual conditions". Indeed, the reality is that contractual conditions have not been modified. The price variation rights, embedded in the contracts, have simply been exercised.
96. Ofcom has not considered whether, in these circumstances, an issue thus arises in respect of GC 9.6 or Article 20 of the Framework. Ofcom has not considered whether it is attributing a failing to GC9.6 which it was not designed to address.
97. Ofcom must consider whether its assessment that GC9.6 needs to be amended pursuant to the Framework is incorrect (and hence whether its justification for the change does not meet the test that Ofcom is required to pass in order to modify GCs (see above/ below).⁶²

⁶¹ Ofcom makes clear that the "material detriment" test is consistent with the law in its assessment in 2011⁶¹: "Ofcom considers that such a threshold is still relevant and likely generally to reflect current consumer protection in this area³⁷. That is, under the UTCCRs contract terms are unfair if, amongst other things, they create a "significant imbalance" in the consumer's (subscriber's) and supplier's (CP's) rights and obligations under the contract. Contract terms which could allow a supplier to change the contract in a significant way could well unbalance the contract and are under strong suspicion of unfairness. This is reflected in the provisions of paragraphs 1 (j), (k) and (l) of Schedule 2 of the UTCCRs, which say that various terms providing for contractual variation may be unfair. Retaining a "material detriment" requirement would therefore generally reflect the "significant imbalance" requirement used to determine the unfairness of relevant contract terms³⁸" [§7.17]

⁶² Although at [§1.31] Ofcom appears to suggest that amending pursuant to the Framework is not the prime focus, but rather an associated one: "modifying GC9.6 as proposed under this option would also be consistent with the express requirements of the Universal Services Directive."

Ofcom's proposed intervention fails to satisfy Section 47 (2) of the Communications Act

Ofcom's proposal to amend GC9.6 is not objectively justifiable

98. Ofcom's justification for revisiting GC9.6 is that the volume and nature of the complaints identified in the Consultation is such that Ofcom believes the approach it took in 2011 has not prevented consumer harm arising. It therefore wishes to revise GC9.6:

"...there is consumer harm that is not being addressed by the combination of existing consumer protection laws and the current requirements of GC9.6. On that basis, the modification would be objectively justified". [§6.53]

99. However, for the reasons discussed elsewhere in this response:

- i) The law already addresses Ofcom's concerns. As Ofcom notes [§3.18 and §3.19] existing OFT Guidance makes clear that a degree of flexibility in pricing may be achieved fairly in a number of ways⁶³. [§3.20] such as *"...specifying the level and timing of any price rise (within narrow limits if not precisely), by linking terms permitting price rises to a relevant published price index such as RPI or by allowing consumers to end the contract and not experience any financial loss as a result of cancellation."* [Emphasis added].
- ii) Ofcom has considered other options, but concluded that its proposed option is the best option for dealing with the harm. Ofcom must thus objectively justify its intervention in relation to the volume and nature of the complaints it has received and it must objectively justify the option it favours in relation to the other alternatives. Ofcom cannot

⁶³ Guidance we followed in respect of our terms

http://www.o2.co.uk/assets2/pdf/2120%20CPM_TandCs_Booklet_LR_ONLINE.pdf

objectively rely on the volume and nature of the complaints evidence to objectively justify its intervention⁶⁴.

- iii) Ofcom has given no consideration to the Law Commission Review and its outcome in relation to providing clarity in the law - yet uncertainty in the law is a justification for Ofcom's action.
- iv) Ofcom already has the tools (in GC23) to address sector specific issues, a regulator committed to least intrusive intervention (as Ofcom is) would objectively favour existing tools.
- v) The degree of "harm" per customer is small (as Which? itself acknowledges), even if one takes Ofcom's assessment that the benefits of price variation are small (which we believe greatly understates the true situation) one is left to conclude that there are no net benefits of intervention – and certainly not sufficient to justify the significant intervention Ofcom proposes, compared with option 1 or 2⁶⁵.
- vi) Ofcom has previously determined that the material detriment test properly implements the USD and is objectively justified. We fail to see how removal of material detriment can be objectively justified when in 2011 its inclusion was justified.

⁶⁴ For example, Ofcom complaints largely relate to one provider rather than the industry as a whole and there is a natural inherent bias in complaints data and Which?'s pledge request such that customer sentiment is not robustly tested (for example, the real question is whether customers prefer the intervention Ofcom proposes and the likely outcomes (for example, automatic risk premium, reduced quality or value, reduced handset subsidy etc.) compared to options 1 or 2. Enders review of Q3 notes: *"Vodafone and EE both improved their gross adds in Q3 with O2 slipping; the latter's boost from the launch of 'On-and-On' may now be wearing off"*. This indicates that customers' priorities are not with the risk of price variation clauses given the publicity associated with Vodafone and EE price rises last year.

⁶⁵ Indeed, RPI is a basket measure in respect of a range of goods and services. Customers are experiencing RPI across a range of products and services. To suggest such rise is material has implications for a wide variety of contracts.

- vii) Furthermore, in 2011 Ofcom explained that the inclusion of “material detriment” was consistent with consumer protection law⁶⁶ and yet now, Ofcom argues it is not. To remove a test on grounds it fails to address the objective of consumer law when just two years previously Ofcom expressly included it in order to reflect consumer law is inconsistent policy making.
 - viii) We believe there is clear guidance in respect of price variation clauses (as discussed elsewhere). We fail to see how Ofcom can now conclude otherwise.
 - ix) Ofcom proposes to apply its intervention to non subscription prices outside the bundle, notwithstanding that it has few complaints in relation to such charges.
100. We believe Ofcom has erred in its Impact Assessment (as we discuss in Section 6) and that in light of that, Ofcom cannot objectively justify the intervention it proposes.
101. In short, an objective assessment would, we believe, conclude that if intervention is justified, any harm identified would be better served via an amendment to GC 23 to address the “unfair surprise” Ofcom identifies (since this does not risk the “unintended consequences” that Ofcom’s proposes solution may cause). A review of GC9.6 could then be undertaken in light of the outcome of the Law Commission review (if necessary). Ofcom already has the tools at its disposal to address the harm of “unfair surprises”. Both its own Better Regulation Principles and the CAT’s profound and rigorous assessment test require that Ofcom takes the least interventionist approach to address the harm identified.

⁶⁶ “Retaining a “material detriment” requirement would therefore generally reflect the “significant imbalance” requirement used to determine the unfairness of relevant contract terms”. [§7.17]

Ofcom's proposal to amend GC9.6 must be not such as to discriminate unduly against particular persons or against a particular description of persons

102. Ofcom explains that the modified condition would apply to all Communications Providers as defined in GC9.6 and as such it would not discriminate unduly against particular persons or against a particular description of persons.

103. The effect of Ofcom's proposed amends to GC9.6 is to make terms which would otherwise be lawful under the UTCCRs, a breach of the General Conditions.

104. This is unsound in a number of respects:

- i) It means some players competing for customers' communications business will be subject to Ofcom's "additional rules" (ECS and ECN providers) whilst others, providing non GC regulated products, will not⁶⁷.
- ii) It means players who offer content/ information society services bundled with ECS/ ECN services will be able to vary the prices of the non ECS/ ECN elements of the bundle under the UTCCRs without customers being able to cancel their contracts without penalty. However, providers without non ECS/ ECN service offerings will be constrained by the General Conditions framework.

105. In breaking the link and consistency between GC9.6 and the UTCCRs, Ofcom's intervention applies to providers to differing degrees depending on the breadth of bundled services they offer and the degree to which the provider is subject to third party cost increases.

⁶⁷ Enders remarks: *Mobile voice and text volumes are looking increasingly vulnerable in the medium to long term given the global growth of OTT communication platforms such as WhatsApp, as discussed in our upcoming report, *Pre-Christmas mobile platforms update: The end of the beginning of the platform wars* [2012-119]

Ofcom's proposal to amend GC9.6 must be proportionate to what it is intended to achieve

106. The Competition Appeal Tribunal explains:

"The principle of proportionality requires that any action by OFCOM shall not go beyond what is appropriate and reasonably necessary to achieve their stated objectives. Also, where a choice exists between equally effective measures that might be adopted to address a problem, recourse should be had to the least onerous measure that will achieve the stated aims. The requirement that OFCOM have regard to the principle of proportionality in performing their duties is set out in section 3(3) (a) of the CA 2003." [51]

107. Ofcom's proposals fail to meet this test in a variety of areas. Ofcom identifies three objectives: mitigate surprise, provide the ability to avoid price rises and mitigate financial hardship.

- i) In respect of surprise, the ASA has already ruled in respect of advertising⁶⁸, the issue is well publicised and Ofcom's option 2 would address surprise, whilst option 4 does not.
- ii) In respect of avoiding a price rise, the existing rules provide for this where there is material detriment. However, Ofcom wishes to go beyond the law. This is a significant intervention and given the complaints data highlights the volume of complaints largely (80%) relate to one provider, option 4 is not a proportionate response.
- iii) In respect of financial hardship, Ofcom has made no assessment in respect of individual customers (and Which? explains this is small in any event). In the absence of such assessment, Ofcom cannot have properly assessed that its intervention is proportionate. As Ofcom acknowledges, the law is clear that price variation clauses are fair

⁶⁸ And we have amended our advertising accordingly.

provided they are in certain form. The Law Commission Review makes clear that the size of increases is an important factor.

- iv) Were intervention to be justified, complaints data shows equivalent volumes for surprise and objecting to price variation regardless⁶⁹. Accordingly, either option 2 or 4 would be effective in addressing harm overall (as measured by complaints). Ofcom should have recourse to the least onerous measure in these circumstances. However, Ofcom pursues the most onerous measure.
- v) Ofcom explains that for the reasons set out in the Consultation, it believes the other options fall short of what is required and that its solution (option 4) imposes no greater regulatory burden than necessary to do so. Since 24% of complainants raises specific concern about lack of transparency. Option 2 would deal with this and Ofcom's concern about "unfair surprises". In respect of these complainants, Ofcom's solution goes beyond that which is required to address their concerns.
- vi) Ofcom judges that its existing powers of enforcement are too onerous/complex to apply. Ofcom's approach is that it is easier to change GC9.6 than enforce the UTCCRs. Indeed, this suggests the very granting of powers to Ofcom is defective. However, Ofcom's proposal to call for fresh enforcement powers (GC enforcement powers) appears disproportionate given that the Law Commission does not suggest exercise of enforcement powers is overly burdensome, indeed it concludes there is a robust enforcement framework:

"Importantly, the UTCCR, unlike UCTA, may be enforced by public bodies as well as individual consumers. They permit the Office of Fair Trading (OFT) and a list of 11 other "qualifying bodies" to go to court to prevent unfair terms from being used.

⁶⁹ 25% and 24%, see §2.8.

These preventive powers have proved to be an important way of regulating the market.” [§2.11] and “The UTCCR impose duties and grant powers to these public enforcement bodies.¹⁴ Additionally, Part 8 of the Enterprise Act 2002 puts in place “a further layer of support” by giving enforcement bodies strengthened powers to obtain court orders (known as “enforcement orders”) against businesses which do not comply with the UTCCR.⁷⁰ [§2.12]

Ofcom’s proposal to amend GC9.6 must be transparent in relation to what it is intended to achieve

108. We find Ofcom’s proposal fails in a number of respects here:

- i) Ofcom’s proposal is to apply a stricter test to communications providers than applies generally. However, its application is uncertain in relation to certain prices as we explain in our comments in response to section 5 of the consultation. As such it is not sufficiently transparent.
- ii) Ofcom has not satisfactorily considered the impact on customers, particular in relation to market outcomes. It is certainly not transparent to customers what the outcomes may be. We note Which?’s pledge website provides no explanation that there could be other outcomes for customers such as reduced handset subsidies or tariff re-structuring or increases in headline prices reflecting risk premiums.
- iii) Ofcom explains that “*Modifying GC9.6 as proposed under [option 4] would also be consistent with the express requirements of the Universal Services Directive.*” [§1.31]. As explained above, given that Ofcom has previously determined that the current regime is also consistent with the USD, Ofcom’s approach gives rise to considerable questions of regulatory certainty and consistency. Equally, Ofcom’s other options, which involve retaining the “material detriment” test, must also be consistent with the USD. Ofcom cannot claim it is required to make the changes because of

⁷⁰ http://lawcommission.justice.gov.uk/docs/unfair_terms_in_consumer_contracts_issues.pdf

the USD. It has already made changes which it recognises correctly implemented the USD. Under the existing implementation, the UK customers benefit from the lowest prices in Europe. Ofcom's justification is inconsistent and conflicting. As such it cannot be transparent.

- iv) Ofcom's own Better Policy Making principles require Ofcom to evidence that its intervention will result in a better outcome in terms of competitive prices overall for customers. No such evidence has been provided. Indeed, given that Ofcom's intervention would make it more uncertain that handset subsidies would be recovered, the outcome is likely to be worse for customers rather than better. The intervention is opaque in this respect – not transparent.
- v) Ofcom explains [§3.23] that “GC9.6 seeks to give consumers similar [to the law] *protection against the effects of price rises (amongst other things).*” It does not. It goes beyond the law. Ofcom suggests it is merely imposing GC9.6 to achieve that which the law intended. That is misleading and as such Ofcom's proposals are not transparent in their presentation.

How other Member States have transposed Article 20(2) of the Universal Service Directive

- 109. Ofcom explains that following its survey of other BEREC members, it notes that of the 13 respondents “*most respondents indicated that subscribers have the right to exit the contract without penalty if the price is increased by any amount.*” 3.12.
- 110. Ofcom makes no mention as to what weight it places on this survey. However, we assume the inference Ofcom seeks to make is that since other Member States have transposed the USD in a particular fashion, then the UK should do so too⁷¹. We think any such conclusion is unsound. Ofcom has

⁷¹ And Ofcom needs to be mindful of the CAT's view on disparate facts. The CAT observed: “*We add that we were referred throughout these proceedings to the position with regard to number portability in other countries, especially Ireland. In our view, as noted by the Tribunal in H3G MCT (at paragraph*

previously concluded that it correctly implemented the USD. We also note Ofcom makes no reference to how the UK compares with these other markets in terms of prices. As Ofcom CEO, Ed Richards, recently announced:

“The UK is the most price competitive mobile phone market in Europe¹. Healthy competition means that UK consumers benefit from better services at lower prices than most other countries in the world.”⁷²

111. Ofcom cannot safely rely on the BEREC survey as evidencing that its intervention is justified.

The Unfair Terms in Consumer Contract Regulations 1999 (“the UTCCRs”)

UTCCRs and General Condition 9

112. Ofcom explains that:

“It is important to note that the UTCCRs and GC9.6 are not the same. The UTCCRs set out the basis on which a contractual term may be considered unfair whilst GC9.6 sets out a requirement which protects subscribers [in the event of any modification of a contractual condition likely to be of material detriment].” [§3.21]

113. Ofcom explains that GC 9.6 “seeks to give consumers similar protection [to UTCCRs] in respect of price rises. [§1.5]. The UTCCRs recognise (as does Ofcom at 1.5) that price variation clauses can be fair in certain circumstances – and hence termination without penalty is not an automatic right in those circumstances.

114. However, as we explain elsewhere, Ofcom removes the possibility that price variation clauses can be invoked without a right to terminate without penalty.

[261]), it is difficult to draw any firm conclusions derived from disparate facts plucked out of the information about a range of international markets.” [127] *ibid*.

⁷² <http://media.ofcom.org.uk/2013/01/23/bidding-in-4g-auction-under-way/>

As such, Ofcom's GC9.6 is inconsistent with the UTCCRs which Ofcom explain seek to achieve similar fairness.

115. Ofcom appears to see GC9.6 and UTCCRs as complementary rules to achieve similar ends. And that since UTCCRs have been ineffective in protecting customers, Ofcom can plug the gap that the law fails to meet though the amendment of the General Conditions.
116. Of course, the GC which Ofcom proposes to amend was reviewed as recently as 2011 and as Ofcom concluded at the time, it was not found wanting.

Clarity

117. Ofcom states the UTCCRs and General Conditions are not the same (although they have the similar goals) [§3.21]. Ofcom maintains, GC9.6 may seek to achieve "fairness" by virtue of dealing with "modifications" to terms, whilst, UTCCRs seek to address the overall "fairness" of terms.
118. As such, as Ofcom itself explains GC9.6 is about protecting customers from "modifications" to contracts, not the inherent fairness of terms in contracts. However, the Law Commission Review makes clear that the UTCCRs seek to deal with unfair surprises and the associated harm. Again, Ofcom's failure to consider the Law Commission Review and its proposals is unsatisfactory.
119. Accordingly, we find Ofcom's justification for amending GC9.6 confused. Ofcom is proposing to amend GC9.6 by reference to the Framework. However, it makes no assessment as to whether the behaviour (price rises) have arisen from "modifications" to terms or from exercise of terms which are transparent in contracts.

The Consumer Protection from Unfair Trading Regulation 2008 (“the CPRs”)

120. We note Ofcom’s comments.

121. Increasing prices in accordance with the terms and conditions of a contract does not constitute a banned practice under these regulations. Neither customers nor Trading Standards have accused us of breaching these regulations in response to our recent price increase.

Ofcom’s assessment

122. We raise a number of fundamental concerns about the validity of Ofcom’s assessment of complaints data. We do not believe that the volume or nature of those complaints is such as to justify the reversal of Ofcom’s previous approach in respect of material detriment.

PRICE RISES IN FIXED TERM CONTRACTS: CONSUMER HARM (Section 4)**Introduction**

124. Ofcom concludes that consumer harm is being caused in the following ways:

- i) Because consumers do not have an automatic right to terminate their contracts without penalty in the event of a price rise.
- ii) There is inconsistent application the material detriment test in GC9.6.
- iii) There is uncertain application of the UTCCRs in this context.
- iv) There is a lack of transparency of price variation terms at point of sale.

125. Ofcom identifies this harm from complaints to Ofcom⁷³, a review of communications providers' terms and information from stakeholders (including Which?⁷⁴). Ofcom explains that the volume and nature of complaints is of concern.

126. Ofcom concludes that whilst there may be potential benefits of price variation clauses, these are likely to be small and that Communications Providers are better placed to bear the risk of cost increases than consumers.

This response

127. In this section we respond to the above points and explain why we disagree with Ofcom's assessment.

⁷³Complaints to Ofcom's Consumer Contact Team (CCT) – discussed in Section 2.

⁷⁴Ofcom suggests input from stakeholders other than Which? However we do not find any further detail of what this information was – Ofcom should be transparent about what information other than Which? it is relying upon.

Communications Providers ability to raise prices in fixed term contracts without an automatic right to terminate without penalty on the part of consumers⁷⁵

Current Rules

128. Ofcom's key concern is that consumers do not have an automatic right to terminate their fixed term contracts⁷⁶ without penalty in the event of a price rise. Of course, the current rules provide consumer protection where terms are "unfair" under the UTCCRs. Such terms are unenforceable. And OFT Guidance makes clear: *"Any kind of variation clause may in principle be fair if consumers are free to escape its effects by ending the contract"* [§12.4]⁷⁷
129. As we understand it, Ofcom is concerned that since the price changes which have given rise to the complaints are either not "unfair" under the UTCCRs⁷⁸ or not causing material detriment under GC9.6 (or it is not certain such that Ofcom is comfortable taking enforcement action - if they were, Ofcom would presumably have taken action since Ofcom has the power to enforce the UTCCRs directly). So either because there is no contravention of the UTCCRs, or, alternatively, Ofcom does not believe an action could successfully be brought, Ofcom prefers to introduce revised sector specific intervention.
130. For the reasons we discuss, we do not believe that Ofcom satisfactorily justifies its approach.

⁷⁵ In its 2011 consultation, Ofcom said GC 9 applied to Business as well..

⁷⁶ Ofcom must make clear that any revision applies to term contracts of 12 months or above.

⁷⁷ OFT Guidance 311: http://www.ofcom.gov.uk/shared_ofcom/reports/unfair_contract_terms/ofcom311.pdf

⁷⁸ OFT Guidance 311 explains: *"A degree of flexibility in pricing may be achieved fairly in the following ways. • Where the level and timing of any price increases are specified (within narrow limits if not precisely) they effectively form part of the agreed price. As such they are acceptable, provided the details are clearly and adequately drawn to the consumer's attention. • Terms which permit increases linked to a relevant published price index such as the RPI are likely to be acceptable, as paragraph 2 of Schedule 2 to the Regulations indicates, subject to the same proviso."* [§12.4]

Ofcom assessment: consumers legitimate expectations, unfair surprise and failure to allow consumers to avoid unfair surprises

131. Ofcom concludes that consumers have a “legitimate expectation” that, like the contract length, prices should be fixed [§4.12]. Ofcom concludes that the UTCCRs are not delivering on this “legitimate expectation” and so the right course of action is for Ofcom to intervene with sector specific regulation in the form of a revised GC9.6.
132. We believe Ofcom’s approach has a number of significant flaws:
- i) Ofcom’s view on consumers’ legitimate expectations is inconsistent with the OFT, Parliament and the Courts. As we explain elsewhere, the OFT and UTCCRs (enforced by the Courts⁷⁹) consider that price variation terms can be fair in relevant circumstances⁸⁰. The legislature has set the rules in a manner deemed appropriate to meet consumer expectations and in a manner designed to ensure customers are not surprised if a price variation clause is invoked. Since the law allows for the terms which Ofcom wishes to prohibit⁸¹, Ofcom turns to its powers to modify General Conditions⁸².
 - ii) Ofcom appears to suggest that customer complaints demonstrate this “legitimate expectation”⁸³. As we explain elsewhere, 80% of Ofcom complaints are in respect of one provider. If Ofcom is to interpret complaints as a barometer of consumer expectation (and we do not

⁷⁹ Ofcom has been clear on many an occasion that it is ultimately for the Courts to interpret the UTCCRs. If the courts disagreed they would themselves find that such terms were unfair.

⁸⁰ Indeed, Ofcom recognises this.

⁸¹ As we explain elsewhere (and as Ofcom recognises) the current law does not prohibit price variation terms in fixed term contracts without an automatic right to terminate without penalty. Such clauses are fair provided they meet certain criteria. the law does not require that price variation clauses which meet those criteria must also provide consumers with an automatic right to terminate without penalty – although, OFT Guidance 311 deals with this aspect at 12.4.

⁸² Ofcom concludes that consumers must always be able to terminate without penalty. The UTCCRs provide that a term is unenforceable where unfair – and price variation terms, provided they meet certain criteria can be fair, and hence enforceable without automatic right to terminate.

⁸³ We understand (although, Ofcom does not say explicitly) that the evidence of “consumer expectations” in this respect is drawn from the complaints, Which? and stakeholder engagement to which Ofcom refers.

accept the data can be relied upon in this respect because of its inherent bias – see elsewhere), then the most Ofcom can argue is that it is a barometer of those complaints arising from the actions of one provider and their terms.

- iii) Ofcom's interpretation that there should be an automatic right of termination where a term (e.g. price variation) is unfair fails to consider that under the UTCCRs the unfair term is unenforceable. But this does not mean that the contract itself cannot continue if it is capable of continuing. Ofcom argues contract termination is the automatic solution. However, as the Law Commission Review makes clear:

"Regulation 8 of the UTCCR states that if a term is found to be unfair, it "shall not be binding on the consumer". The rest of the contract "shall continue to bind the parties if it is capable of continuing in existence without the unfair term". [§2.34]⁸⁴

- iv) Ofcom explains that consumers should be protected from "unfair surprises". The Law Commission Review also makes this clear: *"it is important that unfair terms legislation continues to fulfil its primary role, which is to protect consumers against unfair surprise. Unfair terms legislation cannot, however, solve all the problems of the market place and it should not protect consumers against the consequences of their own poor decisions."* [§3.4]
- v) Ofcom argues that the law is too complicated and uncertain as to provide sufficient protection for consumers (i.e. it is failing to meet consumers' legitimate expectations). Ofcom suggests that it is this uncertainty which now requires Ofcom to step in with a General Condition. The Law Commission Review itself notes concern has arisen about interpretation of the price element aspects of the law following the 2009 Supreme Court decision in relation to the OFT and the banks case. It has also proposed clarification of the "Grey List" of

⁸⁴ http://lawcommission.justice.gov.uk/docs/unfair_terms_in_consumer_contracts_issues.pdf

terms which may be unfair in some circumstances. Again, one of Ofcom's concerns (uncertainty of the law) is being addressed⁸⁵ (although, as we explain elsewhere, OFT Guidance 311 is clear in respect of price variation clauses). Indeed, we are not clear why Ofcom does not seek to address any concerns about clarity via the Review. This would be the place to address the matter rather than through Sector Specific regulation⁸⁶. We suggest that it is not the complexity or uncertainty of the UTCCRs in respect of the material detriment test that is at issue. The law recognises the "material detriment" test and it is very clear that price variation clauses can be fair provided they are transparent and clear⁸⁷ (e.g. the amount and frequency of any variation): i.e. that they are designed such that customers should not be surprised should the variation arise etc. Provided these rules are met, there is no automatic right to terminate without penalty. Indeed Ofcom recognises this at §4.42 to §4.45 of the Consultation.

133. In order to modify General Conditions, Ofcom must provide robust justification in accordance with section 47 of the Communications Act. We discuss this test in more detail in our comments on Section 3 "Legal Framework". We explain why we believe Ofcom has failed to meet that section of the Act.
134. Ofcom suggests that the 'ineffectiveness' of the current regime has been bought to its attention in light of the price variations referred to in Annex 7. Of

⁸⁵ "We think that under the current law, the exemption from the fairness assessment set out in Regulation 6(2) does not apply to price escalation clauses, early termination charges and default charges. This follows from the decisions in *First National Bank*,² *Ashbourne*³ and *Nemzeti*,⁴ and from the statements in *Office of Fair Trading v Abbey National plc*⁵ concerning the grey list. In the interests of certainty, we think that it would be helpful if the legislation stated in clear terms that the exemption does not apply to these terms. This does not mean that such terms are always unfair. Many are perfectly fair, but we think that a court should be able to assess them taking into account the amount of the charge and what the trader provides in return." [§8.4]. Emphasis added.

⁸⁶ Indeed, as the Law Commission explains, the UTCCRs have previously been applied in the mobile market: "An example of the use made of the UTCCR can be seen in the mobile phone market. In 1996, the OFT undertook an investigation into the terms used in standard form mobile phone contracts. These included terms relating to the lack of a "cooling off period", the length of time that consumers were tied into the contract, and the fees payable for disconnecting a service." [§3.18]. To suggest that the UTCCRs are ineffective is not supported by history.

⁸⁷ Ofcom concludes this is unfair – even though OFT Guidance makes clear that such terms can be fair.

course, the intent of the current rules⁸⁸ and the issues arising from the realities of ‘consumer behavioural biases’ have been recognised for some time. Indeed, as the Law Commission Review notes:

“In the last five years, some economists have doubted the model of a rational consumer. A growing literature suggests that consumers display “behavioural biases” which lead them to make “predictably irrational” decisions.”

135. Ofcom argues that market behaviour since 2011 has caused it to revisit its approach to GC9.6. However, Ofcom determined that retention of the material detriment test in relation to price variations was appropriate in 2011. Is Ofcom suggesting that it did not consider that the material detriment test would be relied upon? We presume not. We see no reason why the test should be any less certain now than when Ofcom considered it safe in 2011.

Ofcom’s complaints data does not provide robust evidence for Ofcom’s proposals

136. We have a number of fundamental reservations about Ofcom’s assessment of the complaints data.
- i) Ofcom relies on assumption rather than evidence to support its key concern. Ofcom explains at [§4.5] that *“It seems to Ofcom a fair assumption that most, if not all, of [the 266] consumers made [the complaint of “unfairness”] because they had been notified of the price increases while not being give notice that they had the ability to withdraw from the contract without penalty”*. Since Ofcom explains that this aspect is its key concern, and furthermore that it has undertaken a review of providers’ price variation terms, we are not clear why Ofcom relies on assumption here. It would seem a relatively simply exercise

⁸⁸ *“Unfair terms legislation assumes that consumers are rational but busy. They do not have the time or resources to plough their way through the many standard form contracts they are given. On the other hand, if consumers are told about the price or the subject matter the legislation assumes that they will take these terms into account when choosing whether to enter into the contract. The terms will be subject to competition and should not be assessable for fairness.”* [§3.54] Law Commission Review.

to sample a representative number of those complaints to test its assumption.

- ii) Complaints data has an inherent bias. It must be recognised that assessing consumers' perception of "unfairness" from a population of complainants is not going to provide a balanced, unbiased sample. It is, by definition, going to show that complainants consider the terms about which they are complaining "unfair"⁸⁹. The sample is 'self selecting'.
- iii) Ofcom fails to consider the wider context and consumer benefit⁹⁰. Consumer appreciation of the levels of handset subsidy within term contracts is generally low – and unlikely, we suggest, to be taken into account in any expression of "unfairness" in complaints to Ofcom. For example, taking Ofcom's Consumer Experience Survey [as a control] shows that overall customer satisfaction is generally high. Ofcom acknowledges in its Consumer Experience research that the bargain a customer strikes for a fixed term contract includes the benefit of a heavily subsidised device.
- iv) Ofcom has not provided customer survey data which seeks to test customers overall perception of fairness – being clear about the wider nature of the bargain⁹¹. Neither does Which?'s campaign site.⁹²

⁸⁹ Indeed, As Ofcom recognise, the issue is one of consumer assumption that fixed term means fixed price: "Ofcom understands the frustration that consumers feel when faced with price rises in what they assume to be a fixed contract with a fixed price." <http://advicetoofcom.org.uk/blog/2012/10/ofcom-set-investigate-mobile-phone-and-broadband-price-hikes>.

⁹⁰ Indeed, the Law Commission Report makes this clear:

"We think that under the current law, the exemption from the fairness assessment set out in Regulation 6(2) does not apply to price escalation clauses, early termination charges and default charges. This follows from the decisions in First National Bank,² Ashbourne³ and Nemzeti,⁴ and from the statements in Office of Fair Trading v Abbey National plc⁵ concerning the grey list. In the interests of certainty, we think that it would be helpful if the legislation stated in clear terms that the exemption does not apply to these terms. This does not mean that such terms are always unfair. Many are perfectly fair, but we think that a court should be able to assess them taking into account the amount of the charge and what the trader provides in return." Emphasis added.[§8.4]

⁹¹ For example, Which? recognises that handsets are subject to significant upfront subsidy which thus needs to be recovered over the life of the contract.

137. There is an inherent natural bias in the data Ofcom relies upon. It is simply not robust to rely on data with inherent natural bias for policy making.
138. Judgement of fairness should be taken in a balanced fashion (as the law seeks to do). To assess it based on a complainant's perception of fairness at the point of complaint includes a natural bias and is self-selecting. It ignores those customers who have not expressed a view of unfairness/ fairness.
139. We note that Ofcom concludes that the volume and nature of complaints indicates that the law has got the balance wrong. If that is the case, then the appropriate route to address that would be via a review of the law itself, as the Law Commission is indeed undertaking. However, Ofcom makes no mention of this review. Instead, it seeks to rely on additional regulation⁹³.

Which? Fixed means Fixed campaign

140. Ofcom notes that Which? argues if a mobile operator sells a contract as fixed, it should not just be fixed in term but also other key terms such as service offerings (minutes, texts and data) and price should be fixed too.
141. Of course, that is too simplistic an analysis since on that basis customers would not benefit from price reductions or other new benefits or offers mid term.

⁹² And Which?'s current "pledge" page provides no opportunity for customers to express any concern about the potential implications of any of the solutions. <http://www.which.co.uk/campaigns/technology/fixed-means-fixed/ofcom-consultation/> Not does Which? explain the possible consequences of the intervention.

⁹³ As we explain elsewhere, hence Ofcom makes no attempt to determine if the Law Commission Review might address the concerns Ofcom raises about the failure of the current UTCCRs to provide consumers with the necessary protection.

The scope of Ofcom's approach

142. We note that Ofcom's proposed amendments to GC9.6 is in respect of "*the currently identified harm in relation to price rises – be that a rise in the actual price or a change (e.g. in allowance etc.)*" which would effectively constitute an increase in the unit price paid. For non-price variations, the material detriment test would remain.
143. We have the following reservations:
- i) The effect of this is uncertain – does it encompass a change with only effects unit price? Or if functionality of a service was changed/ removed such that a consumer considered they were worse off, is that included? Where does "price variation" stop and "other term" start. Ofcom gives no consideration to the cooling effect this might have on in life tariff evolution (since providers may be reticent to change anything for fear it will trigger a contract break).
 - ii) The effect is circular. Where a provider cannot control wholesale charges (e.g. 08), then faced with the choice of absorbing a wholesale price increase or increasing retail prices and risk customer termination, a provider might conclude that the best course of action is to bar access to the service concerned. If Ofcom considered this to mean customers were getting less for their money and hence constituted a "price rise" such that they can terminate, this then means that providers options to deal with the increased risk are limited (which naturally inflates risk premium or reduces handset subsidies to the customer depending on outcome).
 - iii) Ofcom risks the price variation intervention applying in circumstances where it has "*not identified any widespread consumer harm in relation to non-price variations*". Ofcom is speculatively seeking to regulate against something which has not caused consumer complaints. Indeed consumers might prefer changes to allowances compared to

increased risk premiums or reduced handset tariffs or upgrade offers. Ofcom anticipates consumer response without substantiating evidence.

144. As such, Ofcom's proposed modification is flawed.

Assessment of the scale of consumer harm

145. Ofcom assesses that the scale of consumer harm is not outweighed by the benefits of price variation clauses.

146. We have a number of reservations about Ofcom's assessment and we conclude it has a number of limitations which mean it is an unreliable assessment. It does not withstand the profound and rigorous scrutiny demanded of Ofcom policy making.

- i) Ofcom does not offer any assessment or quantification of whether actual material detriment/ financial hardship is being caused on an individual basis, and if so, the size (pence per individual) of that harm. This is notwithstanding that at the outset Ofcom explains:

"16% of consumers complained specifically about the harm arising from the amount of the price rise and how it could result in material detriment and/ or financial hardship." [§2.8]

- ii) Accordingly, Ofcom can only say harm "could" be caused. This is not a robust basis upon which to intervene. Annex 7 of the Consultation shows that Ofcom clearly has raw material to assess the impact on a customer basis⁹⁴. Even a rudimentary analysis could allow Ofcom to undertake some analysis of the impact on an individual customer

⁹⁴ As the Law Commission Review remarks in respect of Price Escalation clauses: We thought that it would be difficult to review the fairness of a price escalation clause without considering its amount. "A term permitting a small escalation may be fair: a term permitting a large escalation may be unfair. It would be difficult and artificial to assess the fairness of the term without taking into account the size of the escalation". [§4.25]

basis. Ofcom has made no attempt to articulate what that size of the impact is per customer.

- iii) Without such analysis, Ofcom can only speculate that the current GC9.6 is insufficient. If Ofcom has not undertaken a calculation to consider if any of the price rises have resulted in financial hardship or material detriment, how can it have concluded that GC9.6 has not been engaged (or indeed the UTCCRs have not been engaged). Ofcom has made no attempt to assess whether an RPI increase is causing “material detriment” or financial hardship⁹⁵.
- iv) Ofcom could also make some assumptions about average handset subsidy by way of a proxy to compare the “harm” against the “benefit”. This would be instructive. We fail to see how a robust impact assessment can be made and judgement exercised as to the objectivity and proportionality of Ofcom’s options.⁹⁶
- v) Whilst Ofcom does not seek to quantify harm or benefit on an individual basis, Ofcom discusses the “magnitude” of consumer harm on an aggregate basis, but again makes no attempt to quantify the magnitude because it does not have data that will assist it. It is not clear why Ofcom has not sought this data. Neither is it clear why Ofcom has made no reference to metrics in respect of benefits. For example, the competitive nature of the UK mobile market is clear (see references elsewhere).

⁹⁵ Which? itself comments: “Customers were shocked at the rises - although the money involved is relatively small, no one expects a ‘fixed’ contract to increase in price.” [Emphasis added] <http://www.which.co.uk/campaigns/technology/fixed-means-fixed/pledge-your-support/> And OFT 311 makes clear RPI based variations can be fair. Were RPI to result in material detriment this would have implications across a wide variety of contracts and goods and services.

⁹⁶ As Ovum observes: “This would likely lead to an evolution of the handset subsidy model, meaning that consumers might no longer be able to obtain a high-end smartphone for free or for a fraction of its value as part of their mobile contract. An alternative could be to further vary the set of tariffs on offer, although this could result in significant confusion for consumers” <http://ovum.com/2013/01/22/will-ofcoms-contracts-proposals-address-consumer-harm-or-bring-about-industry-reform/>

- vi) Ofcom speculates that there is a risk of price rises becoming standard and regular practice because some providers have increased prices more than once since 2011 [§4.16]. Ofcom speculates that the risk of reputational harm from repeated rises is low because competitors have pursued similar policies. This is not borne out by the evidence: EE's recent announcement received publicity despite previous increases and Tesco Mobile's Tariff Promise demonstrates some providers taking an alternative competitive stance⁹⁷. No complaints from MVNO customers are reported in Annex 7 (and Ofcom recognises PAYG orientated players offer alternatives)⁹⁸. Ofcom ignores its own submissions elsewhere. For example,⁹⁹ Ofcom continues to believe that its publication of Complaints tables can have an effect on reputation, as per the article "*Naming and shaming companies with poor service pays off for consumers*" submitted by Ofcom to the "Advice to Ofcom" blog. We do not believe this is consistent with Ofcom's speculation that the risk of reputational harm is low.¹⁰⁰
- vii) In assessing the scale of consumer harm, Ofcom makes no assessment as to the scale of consumer benefit – other than to assert it is small. As we explain above, the levels of subsidy in the market are many multiples of the harm identified. Indeed, the contrary assessment is the reality: the level of benefit customers receive from subsidised contracts far outweighs the harm identified.

⁹⁷ <http://phone-shop.tesco.com/tesco-mobile/about-us/press-releases.aspx>

⁹⁸ Indeed, the customer research Ofcom conducted in regard to additional charges concluded that Personal experience of MCP and ETC was reported at 5% to 10% for MCP and 3% to 5% for ETC. Reasons why the proportion of consumers experiencing ETC being lower than MCP could be due to ETC being waived in some circumstances, or paid by an acquiring supplier, or a consumer changing their mind about terminating. [§5.14] <http://stakeholders.ofcom.org.uk/binaries/consultations/addcharges/summary/addcharges.pdf>

⁹⁹ <http://advicetoofcom.org.uk/blog/2012/10/naming-and-shaming-companies-poor-service-pays-consumers>

¹⁰⁰ Indeed, as the following comment on Which?'s website makes clear kudos can be attributed from behaviour in this area: "*In many of our [Conversations on mobile price rises](#), commenters have consistently pointed to O2 as being the only major provider not to increase its prices – and it has lasted some time despite others raising prices earlier this year. JayMusgraev gave O2 kudos for keeping its prices in check prior to the hike: 'Seems that O2 could steal a march on their competitors'". We see no reason why kudos cannot exist in circumstances where some providers raise prices again.*

- viii) At §4.16, Ofcom fears that RPI price increases will become standard and the norm in the communications sector if it does not act. This appears inconsistent with Ofcom's concerns about "unfair surprises". Indeed, were such behaviour to become the norm, then concerns over "surprises" would fall away (and as Ofcom notes, since the benchmark is generally RPI, consumers would be familiar with the amount of possible rises).
- ix) At §4.18, Ofcom suggests that "arguably"¹⁰¹ if price rises become standard practice, the level of competition on headline prices may reduce because customers will be less responsive to them since they expect price rises and accordingly headline price competition will be dampened. Accordingly, the benefits of price variation clauses which Ofcom identifies at §4.22 would not necessarily flow through fully. Ofcom relies on hypothesis here. The facts are that UK is the most price competitive market in Europe.
- x) At §4.19, Ofcom explains "*Furthermore, uncertainty about future prices could make new customers wary about signing up for new contracts with minimum contract periods, opting instead for pay-as-you-go offers or contracts without minimum contract periods*". However, Ofcom makes no mention as to what consumer harm it believes would arise in this circumstance.

147. For these reasons, Ofcom's assessment fails to demonstrate a profound and rigorous analysis and as such it is unsafe to proceed on the basis Ofcom proposes.

¹⁰¹ Ofcom is in effect relying on a hypothesis.

Communications Providers' inconsistent application of the "material detriment" test in GC9.6

148. General Condition 9.6 currently places a positive obligation on providers to notify and give subscribers the right to withdraw from their contract without penalty in the event of any modification likely to be of "material detriment".
149. Contrary to Ofcom's own assessment, mobile operators have generally been consistent in their application of material detriment test by reference to RPI (and if they had not, and gone beyond, Ofcom would presumably have taken action). Even if there was inconsistency, that could be remedied by Ofcom Guidance.
150. Ofcom acknowledges that RPI is currently a standard benchmark used by some Communications Providers in defining material detriment. Given that OFT Guidance explains that reference to RPI can be fair (see 12.4 of OFT 311)¹⁰², we believe that Ofcom's "inconsistency" argument is significantly overplayed¹⁰³. Indeed, at 4.16 Ofcom remarks:

"Since most providers set a threshold (usually by up to RPI) before they allow consumers to exit without penalty"

151. Given this, it is obtuse for Ofcom to argue that it should remove the "material detriment" test because of "inconsistency". Ofcom fails to demonstrate consumer harm arising from inconsistency. It is not inconsistency that Ofcom is concerned about (since as we say that could be dealt with by Guidance). Rather the issue is whether the price rises are causing material detriment. The test is whether any mobile operator has introduced price rises which result in material detriment. As we explain above, Ofcom makes no such case.

¹⁰² *ibid*

¹⁰³ Indeed at §4.17, it is not clear whether Ofcom is suggesting RPI is too vague? If so, this appears counter to OFT Guidance.

152. Ofcom asserts elsewhere that the nature of price rises cited (see Annex 7) is such that the amount of the price rises is causing consumer harm. Here Ofcom refers to the 16% of complainants who maintained the amount of the increases could result in material detriment/ financial hardship. And here Ofcom says:

“This suggests recent price rises have resulted in material harm for some consumers even where the price rise was less than RPI and/ or whatever other threshold or criteria the provider has applied to identify material detriment.” [§4.30]

153. However, if this is the case, Ofcom fails to explain why it has not taken any action under General Condition 9.6, if it considers that these complaints are justified and that the rises are causing material detriment.

154. Ofcom has either concluded that:

- i) General Condition 9.6 has been complied with in these cases, in which case no material detriment is being caused. In these circumstances Ofcom cannot rely on the 16% in its case to justify action. Since it has already decided no financial hardship is being caused. In this case the assertion elsewhere that the (unquantified) scale of harm requires it to act must also fall away; or
- ii) General Condition 9.6 has been contravened but the level of harm is such that administrative priorities do not require it to act. Again, if the level of harm caused has not been sufficient to justify Ofcom enforcement action, Ofcom cannot now claim that the level of financial hardship caused is significant such that it must now act.

155. In either case, Ofcom cannot now claim that the level of financial hardship caused is significant such that it must now act.

156. Indeed, Ofcom has made no attempt to quantify the degree of financial hardship. That prices have increased in line with the Retail Price Index cannot be sufficient to claim material harm. Ofcom must thus rely on the evidence it puts forward in respect of the 25% of complainants who claimed about the principle and the 24% who complained about transparency.
157. Ofcom is also inconsistent. It explains that price is one of the key elements of the bargain – there being other terms – yet it concludes that the material detriment test is insufficient for price variation terms – yet sufficient for other important terms.

Uncertainty under the UTCCRS

158. Ofcom's suggestion that there is uncertainty under the UTCCRs is misleading in respect of Ofcom's key concern: that consumers should have an automatic right to terminate their contract without penalty.
159. Ofcom explains at §4.40 that OFT's guidance explains that any right for the supplier to unilaterally vary the price is liable to be unfair. Ofcom then goes on to say that this position is complicated or made significantly less certain by the OFT's clear explanation that in some circumstances, price variation terms can be fair. We don't find OFT Guidance "complicates" matters. Indeed we find OFT 311 quite clear in relation to RPI price variations. Ofcom see "complications" because the Guidance simply does not accord with the belief of some customers that there should be an automatic right to terminate. As we explain, the Law Commission Review notes that OFT Guidance provides proposes to retain the "Grey List".
160. Indeed, Ofcom's suggestion that the UTCCRs are uncertain is contradicted by its statement that:

"In other words, both these points indicate that, whilst most terms providing for price rises are likely to be unfair where they do not

provide consumers with a corresponding right to withdraw for the contract without penalty, some such terms may be fair.” [§4.45]

161. Furthermore at §4.53 Ofcom refers to the:

“...clear and straightforward general principles reflected in the UTCCRs.”

162. We would also point out that in its guidance on UTCCRs in 2008, Ofcom referred to OFT guidance 311 and 143 as “*extensive*” and “*comprehensive*”.¹⁰⁴ [§A1.18]

163. Accordingly, Ofcom’s assertion that uncertainty in the UTCCRS is causing consumer harm is doubtful. There is no uncertainty in relation to price variation clauses. It is clear they are permitted provided they meet certain conditions and are thus fair. And in any event, the Law Commission proposes clarification in respect of the “Grey List” (which Ofcom’s proposal would not recognise in relation to services provided under General Conditions).

164. The argument that uncertainty in respect of the UTCCRS is leading to consumer harm is simply ungrounded and is without substance.

Lack of transparency of price variation clauses

165. Ofcom concludes that despite a range of existing rules¹⁰⁵ being in place, there remains insufficient transparency. Moreover, for a number of reasons, it does not appear appropriate to continue to rely on these rules.

166. Ofcom argues that transparency cannot be relied upon going forward because:

¹⁰⁴ <http://stakeholders.ofcom.org.uk/binaries/telecoms/policy/addcharges.pdf>

¹⁰⁵ And indeed, recent ASA rulings make clear the ASA view that advertisers should qualify prices where they can be increased mid term http://www.asa.org.uk/Rulings/Adjudications/2013/2/Vodafone-Ltd/SHP_ADJ_210326.aspx

- i) Rules requiring transparency have not worked to date. We agree that the results of the Which? Mystery Shopping demonstrated confusion amongst retail staff regarding price variation terms. However, notwithstanding this, Ofcom's principle of intervention in the least intrusive manner is not extinguished. Ofcom must still consider whether, for example, an amendment to GC 23 would be an appropriate solution rather than amending GC 9.6.
- ii) Transparency rules are uncertain. Given informed, empowered consumers are at the heart of consumer law, to suggest that transparency rules should not be relied upon because they are uncertain is unconvincing. Indeed, on that basis, GC 23 (and all other General Conditions seeking to provide transparency) should be removed because of their uncertainty. In that case, by Ofcom's own admission, their previous introduction must be unsafe because they cannot be relied upon to "*establish in any particular case that consumers were not provided with the relevant information*". [§4.68]. As such, their introduction could not be objective or targeted since they would be uncertain to address the issue.

Ofcom fails to explain why it cannot take action already

167. In 2008, Ofcom explained:

"Unfair terms are not binding on consumers and it is open to consumers themselves to challenge in court terms they consider unfair. In addition, under the Regulations the OFT, or a qualifying body such as Ofcom, has a duty to consider any complaint it receives about unfair standard terms. Where that body considers a term to be unfair, it has the power to take action on behalf of consumers in general to stop the continued use of the term, if necessary by seeking an injunction in England, Wales and Northern Ireland or an interdict in Scotland. "[§A1.20]"¹⁰⁶

¹⁰⁶ <http://stakeholders.ofcom.org.uk/binaries/telecoms/policy/addcharges.pdf>

168. Ofcom appears to have either concluded no contravention of the current law is taking place, or that, for whatever reasons the recourse set by parliament is too burdensome. Accordingly, the most convenient course of action is to intervene with a regulation GC.
169. We do not consider this is a robust justification for intervention given the implications of such intervention (see elsewhere).

Who bears the costs?

170. Ofcom concludes that “*Communications Providers should generally bear the risks of cost increases during the lifetime of fixed term contracts*”. Of course, this belies the reality; the market is likely to transfer the risk to consumers in one form or another (for example, headline prices increasing to hedge risk). We discuss these possible outcomes below in relation to section 5 of the Consultation.

PRICE RISES IN FIXED TERM CONTRACTS: OTHER ISSUES (Section 5)**Summary**

171. In this section we respond to the number of related issues Ofcom identifies in the Consultation.

The different price elements in a contract

172. Ofcom acknowledges that “*most of the complaints made to us and via Which? appear to relate to monthly subscription charges*”. [§5.7] However, Ofcom concludes that this is not a reason to treat other prices charged under the contract differently (e.g. out of bundle, additional services, administration charges). Furthermore, Ofcom argues it would defeat the key principle that Ofcom is seeking to address – consumers’ ability to avoid price rises during fixed term contracts.[§5.9].

173. Ofcom’s assessment fails to meet the test set at section 47 of the Communications Act, for example:

- i) Ofcom’s concern is that customers cannot avoid price increases. This logic does not apply to the case of non-subscription services because customers can avoid or reduce such charges by controlling their consumption of such services. Accordingly, customers can also limit any harm (financial hardship) in the same manner.
- ii) Ofcom justifies its intervention based on the volume of complaints. However, Ofcom acknowledges “*most of the complaints made to us and via Which? appear to relate to the monthly subscription charge*”. [§5.7]. This is not surprising: subscription price increases are a relatively recent phenomena that, by definition, have affected all customers with subscriptions. They have drawn significant media attention. Conversely, price increases for other services affect a minority of customers; they are a well-established practice that customers appear to understand and which, as Ofcom acknowledges,

have not generated significant complaints. Ofcom provides no evidence of harm in relation to non-subscription prices. Ofcom's approach is simply "why shouldn't they be caught"¹⁰⁷?

- iii) Ofcom must also recognise that a variety of services, such as Premium Rate Services and International Roaming services are already subject to specific regulation (and separate terms). International Roaming pricing is already subject to considerable regulation. Indeed, Ofcom has recently suggested that this has resulted in reductions in complaints.¹⁰⁸
- iv) We would also point out that Ofcom has already assessed and dealt with any harm in respect of "additional charges" in its Consultation and subsequent Statement¹⁰⁹, wherein it concluded that, amongst other things, Early Termination Charges were fair if they reflected any costs saving a provider made by virtue of the consumer terminating early and they did not mean the provider was placed in a better position than if the contract ran its term.
- v) Ofcom maintains its proposals are to the benefit of customers. In Telefónica's view, introducing regulation in the form of the proposals described in option 4 in respect of non-subscription charges is likely to result in a worse outcome for consumers. Where providers are faced with escalating third party wholesale charges a possible course of action may be to remove those from the bundle or simply close access to them (whether in bundle or non-subscription) or increase the relevant risk premium in retail prices. We do not see how this outcome is beneficial for customers or meets Ofcom's objectives.

¹⁰⁷ We note Ofcom's confirmation that this does not mean that the consumer should be able to withdraw without penalty from the main contract for services, only the separate "bolt on" contract. [§5.18]

¹⁰⁸ "The March 2012 Statement reported that the CCT had received a lower level of complaints in relation to roaming inside the EU, compared with outside, which suggested that the Roaming Regulation had been successful in addressing consumer harm caused by roaming inside the EU. Although roaming complaints to the CCT continue to mainly relate to roaming outside the EU, all roaming complaints have fallen approximately 25% in recent months. This is a positive sign and suggests that the recast Roaming Regulation may already be having a positive effect. " [1.10]

¹⁰⁹ <http://stakeholders.ofcom.org.uk/binaries/consultations/unexpectedly-high-bills/statement/report.pdf>
<http://media.ofcom.org.uk/2008/02/28/curbing-unfair-additional-charges-on-consumers-bills/>

174. As Ofcom acknowledges, the statutory test for amending the General Conditions is set out in section 47 of the Communications Act. Modifications must, amongst other things, be objectively justifiable and proportionate. Furthermore, Ofcom's policy for any intervention is that it should be targeted at areas that are causing consumer detriment. As we explain above, Ofcom's proposals in respect of non-subscription charges do not meet the relevant test. Ofcom must rethink its approach here.

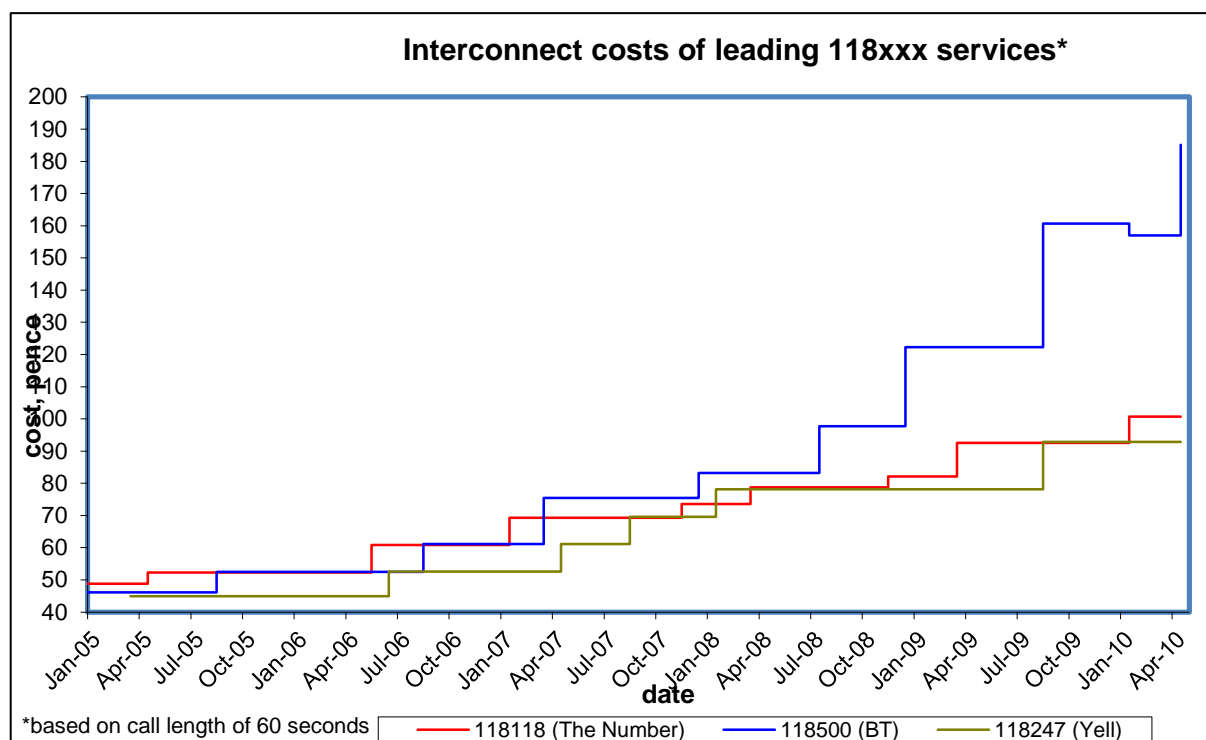
Protecting business customers from price rises in fixed term contracts

175. We note only a small fraction of complaints (20 out of 1644) Ofcom received were from business customers but that Ofcom intends that its proposal will apply to domestic and small business customers (up to 10 employees) who are on non-negotiated contracts. This being consistent with the existing GC9.6.
176. We agree that notwithstanding the low number of complaints, the definition of small business customers should be consistent with that Ofcom adopts in the other parts of the General Conditions.

Allowing Communications Providers to increase prices for reasons outside of their control

177. We note Ofcom's view that Communications Providers are able to take steps to mitigate the risks in respect of wholesale price changes outside of their control.
178. The reality is the more unpredictable the changes the greater the risk premium providers will have to build into tariffs, or alternatively, providers may terminate access to those services (see above). Clearly, if providers cannot safely terminate access without triggering material detriment and a customer's right to terminate without penalty, then this may be reflected in the risk premium or elsewhere.

179. Originating communication providers set retail prices for a variety of services, including premium rate services and other revenue generating services on non-geographic numbers¹¹⁰. The wholesale prices for some of these services can vary quite substantially over time. For example, the following graph sets out the increasing wholesale charges for the leading directory enquiry services from 2005 - 2010



180. Ofcom will note the frequency and size of the wholesale price increases.
181. Clearly, as Ofcom notes in §5.12, originating communication providers are in a good position (relative to consumers) to understand the risks of wholesale price increases. If retail customers are permitted to withdraw from minimum contract terms should an originating communication seek to pass through an increase in wholesale charges, the originating communication provider is likely to increase retail prices at the outset of the agreement based, perhaps, on a worst case view of potential wholesale charge increases that it might be subject to. Alternatively, the originating communication provider might seek to deny its customers access to the service, altogether if the wholesale charge rose. Either outcome (an immediate price increase or the subsequent

¹¹⁰ Including 08x numbers and 118xxx

denial of service) would, Telefónica suggests, be an unfortunate consequence of regulatory intervention.

182. On a related point, under Ofcom's proposals to introduce "disaggregation" in respect of the provision of services delivered by way of non-geographic numbers¹¹¹, customers would pay a "service charge" for the service itself, and an "access charge" for the access to the service, including the conveyance of the call. Telefónica assumes that, if Ofcom implements its proposals in that consultation document and this one, then a change in the service charge would not trigger a customer's right to terminate the agreement with the originating communication provider. This must surely be the case; under disaggregation, the originating communication provider has no role at all in setting the service charge. It simply cannot be reasonable to put the originating communication provider at a commercial disadvantage by virtue of decision made by the non-geographic service provider to increase the service charges clarification of the matter. If Ofcom's intention *is* to allow customers to withdraw from their contract with the originating communication provider in the event of a service charge increase, then originating communication providers are likely to consider how best to protect their position by, for example, ceasing to provide access to the relevant services at all. Again, in Telefónica's view, this outcome would not be in consumers' best interests.

183. Accordingly, we believe that third party wholesale price changes outside our control should be excluded. We believe this strikes the right balance for consumers – and avoids significant risk premiums being built into tariffs from the outset.

Price rises to one or more services in a bundle

184. We note that the proposed GC9.6 will apply to those services subject to GCs within any bundle, but not non-GC services (e.g. content).

185. Since non-GC services will continue to be subject to relevant consumer protection law, Ofcom's approach to non GC services will enable bundle

¹¹¹ See: <http://stakeholders.ofcom.org.uk/consultations/simplifying-non-geographic-no/>

providers greater flexibility to deal with underlying cost changes. Furthermore, Ofcom's approach here is inconsistent with its approach in respect of other charges [§5.3].

186. As such, Ofcom's proposal does not apply to all providers in a non discriminatory fashion. Depending on the mix of GC vs non GC services in a bundle, some providers will be in different positions.

How communications providers notify consumers of contract variations

187. We agree with Ofcom that notices should be clear and understandable. We agree with Ofcom that providers are best placed to decide how they communicate contract variations with their customers.
188. We agree Ofcom's approach should be to liaise with relevant providers in respect of the small number of complaints Ofcom receives in relation to the prominence/ clarity of notices (we note 10 complaints about this issue were received [§5.43]).

Timescales set by Communications Providers for consumers to cancel their contract without penalty for contract variations

189. Noted.

OPTIONS FOR ADDRESSING CONSUMER HARM FROM PRICE RISES IN FIXED TERM CONTRACTS (Section 6)

Introduction

190. Ofcom sets out four options¹¹² for addressing the consumer harm identified¹¹³.
191. Ofcom also sets out its assessment of the merits and limitations of each option, provides an assessment of the potential impacts of each option and invites stakeholder responses.
192. We welcome the opportunity to respond. As requested at §6.4, we have also commented on the specific issues Ofcom raises.

Ofcom's conclusion

193. As we explain above, we believe that Ofcom's assessment is inconsistent with the OFT's interpretation of the law – and that it is pre-emptive to make such interventionist changes in the communications sector when the law is itself being reviewed by the Law Commission.
194. Ofcom concludes that current rules are “*not operating effectively to meet their aims, in particular*” [§6.36]:
- i) The rules are not operating to meet customers' legitimate expectations that a fixed term contract means fixed prices;

¹¹² “Option 1: make no changes to the current regulatory framework (maintain the status quo). • Option 2: require greater transparency of price variation terms by Communications Providers and publish Ofcom guidance on the application of GC9.6 and the UTCCRs to price rises and relevant contract terms. Option 3: modify GC9.6 so that consumers have to expressly opt-in to any variable price contract offered. • Option 4: modify GC9.6 so that consumers are able to withdraw from a contract without penalty for any increase in the price for services applicable at the time the contract is entered into by the consumer (including changes to the level of service provided which effectively constitute a (unit) price increase).” [§6.5]

¹¹³ Ofcom also explains that a 5th option: to prohibit price increases in fixed term contracts, would not be consistent with Article 20(2) of the Universal Service Directive and that it would be disproportionate to limit commercial freedom of providers in such a way. Hence it has not been considered further. [§6.2]

- ii) The rules are leaving customers exposed to unfair surprise/ and or unfair effects; and
- iii) The rules are not giving consumers sufficient ability to avoid these surprises and effects (by ending contracts without penalty).

Ofcom's assessment of the options

195. Ofcom considers four options¹¹⁴ and concludes that transparency itself is not enough because it does not automatically enable customers to exit a contract without penalty.

196. In this response, we focus on Ofcom's Option 1, 2 and 4 because:

- i) Ofcom's preference is to intervene only where necessary. Ofcom must give due consideration to Option 1;
- ii) Ofcom makes clear that Option 2 (greater transparency) has much to commend it¹¹⁵; and
- iii) Option 4 is Ofcom's proposed solution.

197. We conclude that the case for Option 4 is not robust and does not pass the test for intervention that is required. We believe Ofcom needs to reflect on this and reconsider Options 1 and 2.

Option 1: make no changes to the current regulatory regime

198. Ofcom is concerned that this option would retain the "*significant discretion to determine (in the first instance) whether the price variation (or other variation) is likely to cause "material detriment to their subscribers and therefore whether the GC9.6 rules would apply"*. We do not agree with this

¹¹⁴ And discounts a fifth option – to ban price variation clauses.

¹¹⁵ "We acknowledge that, given the risks of greater intervention in the market, the case for adopting a transparency remedy would be strong if there were some ambiguity about whether price rises in fixed term contracts can create countervailing benefits for the consumer". [§6.22]

characterisation. Providers do not have discretion to determine whether or not General Conditions apply. Ofcom may believe providers have “significant” discretion but this is not what the evidence shows. As discussed elsewhere, OFT Guidance makes clear the boundaries for a fair price variation term¹¹⁶, and Ofcom has previously accepted that “material detriment” in GC9.6 is consistent with the law. Furthermore, many mobile price variations in Annex 7 are RPI based.

199. Ofcom argues it has “significant evidence” that consumers are not aware of what bargain they are striking in relation to mobile phone contracts (we assume Ofcom means in relation to price rises) [§6.8]. As we explain elsewhere, Ofcom’s assessment of its complaints data is flawed in this respect (for example, 80% of Ofcom complaints are about one provider and 24% overall had assumed “fixed means fixed”). Ofcom could equally conclude that the volume of complaints primarily arises from one provider and that 76% of complainants overall understood minimum contract period did not mean fixed price. So the contrary conclusion to Ofcom’s assessment can be reached from the same evidence as Ofcom relies upon.
200. Ofcom asserts that customers “may” have been inhibited from making informed transactional decisions. That is speculative. As discussed elsewhere, there is significant evidence that UK customers are benefitting from the most competitive market in Europe. Furthermore, at 4.17, Ofcom discounts greater transparency as a solution because it considers it “*uncertain*” and that consumers may consider price variation terms “*less a priority than terms such as contract length, the bundled call minutes or data usage and the size of any handset subsidy*”. Furthermore, that giving greater transparency may overload customers with information. If this is the case, then Ofcom’s concern that informed transactional decision making is being inhibited by the current position is unfounded – the current rules are not inhibiting customers from making informed transactional decisions. Rather consumers are simply making decisions on what they value more.

¹¹⁶ For example, see 12.4 of OFT Guidance 311.

201. Furthermore, for Ofcom to discount Option 1, one has to suspend belief that, notwithstanding the coverage of the issue and the numbers of many PAYM customers who will have experienced the issue, consumers will continue to be “surprised” by price variations. Furthermore, the recent ruling by the ASA requires transparency in advertising.¹¹⁷
202. Accordingly, we find it unconvincing to assert that the “harm” of “surprise” will continue in any material form if Ofcom makes no changes. Quite clearly, any surprise that existed is long gone amongst the general population¹¹⁸.
203. Ofcom concludes that the existing rules (CPRs, GCs 23 and 24 and the UTCCRs) are either not operating effectively or not being sufficiently adhered to in order to protect customers. If the latter is the case, we are unclear why Ofcom has not considered enforcement of the existing rules. If that is the case, it is not that the rules are ineffective, rather it is that enforcement of those rules is ineffective. However, Ofcom seems to suggest that it has not taken enforcement because the law is uncertain. We are not convinced by Ofcom’s assertion that the law is uncertain in relation to price variation clauses (for reasons explained elsewhere) and, in any event, if that is the case, then that is a matter for the Law Commission Review, not sector specific regulation. Ofcom needs to show that urgent action via an amendment to GC9.6 is a necessary and proportionate response to an “uncertain” law. For the reasons discussed elsewhere, Ofcom’s assessment of consumer complaints does not provide a robust basis for such action.
204. Ofcom explains that *“Our review of the Price variation terms, meanwhile, suggests some do not make clear the level and frequency of any Price rise nor the circumstances in which the consumer can withdraw from the contract.”* [§6.8]. Ofcom makes no reference to OFT Guideline 311 which sets out the prerequisites for price variation terms to be fair and, if they are not, then they are unenforceable. Ofcom fails to consider if enforcement of

¹¹⁷ *ibid*

¹¹⁸ Indeed, we note Ofcom does not make any reference to the distribution of complaints over the period and whether the data shows the majority arose with the first announcement.

existing rules could be relied upon – and in particular that terms which fail to meet the current rules are unenforceable.

205. Ofcom identifies that *“This evidence suggests that the fundamental requirements of fairness in relation to price, and of an appropriate balance in the rights and obligations of the parties, which the UTCCRs and GC6.9 seek to reflect, are not being met.”* If the UTCCRs are not being met, then Ofcom has the choice of enforcement action. However, Ofcom dismisses such action on the grounds it is too burdensome and uncertain. Given that Ofcom has previously been clear that the courts ultimately determine fairness under the UTCCRs, we are unclear why this route would be “uncertain” other than of course Ofcom is concerned that the courts will not interpret the law as some complaints might wish.
206. Furthermore, Ofcom ignores the point that the UTCCRs have been shaped by Parliament and the courts (along with OFT guidance) to deliver the fundamental requirements of fairness and an appropriate balance of the rights and obligations of the parties. GC9.6 reflects this with the inclusion of the “material detriment” test. Both are delivering what they are intended to deliver. The issue is that Ofcom now proposes to change the rules to meet a different outcome to that which was intended by Parliament and the courts (notwithstanding that Ofcom agreed with the test in 2011).
207. Ofcom argues that a change to the status quo would also be more consistent with the express requirements of Article 20 (2) of the Universal Services Directive. As discussed elsewhere, Ofcom has already concluded that the current rules meet the USD. The evidence Ofcom relies upon is flawed and to overturn its previous conclusions based on flawed evidence is not objective. Further, given the implications of Ofcom’s proposed intervention, we do not believe Ofcom has given sufficient consideration to its Better Policy Making Principles (discussed earlier).
208. Ofcom argues that consumers have no option but to accept price variation terms. That there is no recourse if price variation terms are unfair. This is not the case, Ofcom fails to consider that if terms are “unfair” they are

unenforceable. Accordingly, the current law already provides resolution since consumers can avoid the effects of unfair terms since they are unenforceable.

209. Furthermore, Ofcom's Principle is flawed since it applies to "potentially unfair terms". If it is to apply at all, it should only apply to "unfair" terms.
210. Given that Ofcom made clear in 2008 that the material detriment test should be retained, we fail to see how Ofcom can properly suggest now that reliance on it demonstrates that there is a "fundamental imbalance". At most, it appears an issue of transparency, that consumers do not appreciate where the law draws the balance. However, rather than consider transparency, Ofcom seeks to redraw the law for the communications sector.
211. Ofcom assesses that *"maintaining the status quo would not address the uncertainty arising out of providers inconsistent application of GC9.6 and or/ the uncertainty of the application of the UTCCRs in any particular case.."* However, Ofcom fails to adequately consider whether Guidance would provide such certainty.
212. In summary, as we discuss above, we find that Ofcom's assessment of this option is unsound and does not meet the profound and rigorous scrutiny required.

Option 2 – require greater transparency of price variation terms by Communications Providers and publish Ofcom Guidance on application of GC9.6 and the UTCCRs to price rises and relevant contract terms

213. Ofcom discounts greater transparency measures because *"consumers may already find the amount of information available to them in the form of advertisements and terms and conditions to be difficult to understand and/ or assess in order to compare offers"* [§6.10]
214. That Ofcom has already cited that the harm being caused is "surprise" must surely mean that any rationale for not introducing greater transparency must be obtuse.

215. At §6.11 and §6.13, Ofcom considers that it could either amend GC 23 and GC 24 to include *“an express requirement for information about price variation terms to be provided at point of sale”* or it could amend its Guidance on these GCs to make clear that such information should be provided. Ofcom concludes that *“This would ensure that consumers are given information that would enable them to know what bargain they are striking in relation to the Price that they would be expected to pay and how this may change over the fixed term.”*
216. And at §6.15 and §6.16 Ofcom recognises the benefits of transparency. Although, confusingly at §6.22 Ofcom goes on to say *“given the uncertainty about whether transparency remedies will be sufficient”*... when earlier at §6.14 it has already made clear they would be sufficient.
217. At §6.17 Ofcom argues that the effectiveness of transparency of price increases is uncertain given the complexity of contracts and the large quantity of information a consumer needs to process. Again, we find this obtuse since, if that were the case, Ofcom should dismantle GC 23 and GC24 because they are ineffective. A Better Policy Making principle is to dismantle ineffective regulation.
218. Ofcom suggests that *“by themselves, measures designed to increase transparency would not provide consumers with sufficient capability to avoid the effects of unfair terms or practices”* [§6.20].
219. Ofcom explains that customers should be able to avoid the effects of unfair terms or practices. Ofcom fails to recognise that:
- i) customers can do so already under the UTCCRs (and under the GC9.6);
 - ii) in the former, where price variation terms do not meet OFT guidance and hence are found unfair and unenforceable, and
 - iii) in the latter (GC9.6) where material detriment is caused.

220. What Ofcom is simply saying is that it does not believe price variation clauses can be fair unless there is an automatic right to exit without penalty. This is not consistent with the law.

221. In conclusion, Ofcom explains:

"We acknowledge that, given the risks of greater intervention in the market, the case for adopting a transparency remedy would be strong if there were some ambiguity about whether Price rises in fixed term contracts can create countervailing benefits for the consumer." [§6.22]

222. Ofcom's Better Regulation Principles¹¹⁹ make clear:

"Sometimes the fact that a market is working imperfectly is used to justify taking action. But no market ever works perfectly, while the effects of...regulation and its unintended consequences may be worse than the effects of the imperfect market"

223. And, as Ed Richards acknowledges:

*"The UK is the most price competitive mobile phone market in Europe¹. Healthy competition means that UK consumers benefit from better services at lower prices than most other countries in the world."*¹²⁰

224. There is clear evidence that there are countervailing benefits of the current UK regime. Ofcom gives no consideration to this. Ofcom errs in its assessment (in that it fails to consider the evidence) and in its decision, since if it had considered such evidence it would not have reached the same conclusion (because there is the clear evidence that UK customers are benefiting from the current regime). The Law Commission Review also makes clear:

¹¹⁹ *ibid*

¹²⁰ *ibid*

“There are no easy solutions to preventing traders from exploiting behavioural biases in the way that they price and promote products. A study for the OFT identifies three possible strategies: competition, learning and transparency.” [3.29]

225. Notwithstanding this, Ofcom discounts these options. Instead it concludes sector specific regulation is necessary.

Option 4 – Modify GC9.6 so that consumers are able to withdraw from a contract without penalty for any increase in the price for services applicable at the time the contract is entered into by the consumer (including changes to the level of service provided which effectively constitutes a (unit) price increase

226. Ofcom explains it's provisional view is that adopting this option is *“necessary and appropriate to secure the fundamental fairness in respect of price (and the ability to avoid price variations in fixed term contracts) that the current rules seek to reflect”*
227. Ofcom argues that the law is not working properly to secure the fundamental fairness it intends to achieve. This is misleading: the law clearly provides that price variation clauses can be fair in certain circumstances and hence there is not an automatic right under law for consumers to avoid price variations without penalty. GC9.6 reflects this with the material detriment test.

228. Indeed Ofcom, OFT, the Law Commission and the Courts recognise this:

“... a degree of flexibility in pricing may be achieved fairly in a number of ways such as by specifying the level and timing of any price increases (within narrow limits if not precisely), by linking terms permitting price rises to a relevant published price index such as RPI or by allowing consumers to end the contract and not experience any financial loss as a result of cancellation.” [§3.20].

229. The reality is the law and GC9.6 are not ineffective as regards their intent: they permit price variation terms which meet certain criteria. It is that which Ofcom seeks to change for the communications industry. Moreover, Ofcom proposes to change it based on flawed evidence and in a manner which does not meet section 47 of the Communications Act.

230. Ofcom argues that the complaints evidence justifies its intervention:

Our evidence and Which?'s research indicates that consumers object to the principle that their Communications Provider has the discretion to increase prices at all when the consumer has already entered into the contract." [§6.35]

231. As we explain in this response, Ofcom errs in its analysis of its complaints data. If Ofcom followed its Better Policy Making Guidance it would conclude that Options 1 or 2 were more appropriate solutions than Option 4. However, Ofcom's solution is in effect to propose to ignore general consumer law, the use of existing remedies (guidance, GC 24, enforcement of UTCCRs (if relevant), its previous assessments in respect of GC 9.6, and to propose to, in effect prohibit (in any other name) the use of price variation clauses that would otherwise be lawful in any other industry. The evidence Ofcom relies upon is flawed and does not justify the intervention it proposes.

232. Ofcom suggests its solution would be consistent with how the majority of other EU Member States have transposed the relevant Directive. This is not persuasive since Ofcom has already determined the current regime correctly implemented the Directive and, moreover, the evidence is clear that UK customers benefit from the most competitive prices in Europe.

233. Ofcom forms the view that any disadvantages arising from changes in the way handsets are obtained by consumers would be outweighed by the protection offered by option 4. Ofcom reaches this conclusion without any robust research to determine customer preferences. For example, Ofcom attempts no research to establish if consumers would prefer option 4 and

paying more upfront for their handset [\$6.41] or option 2 without the outcomes Ofcom anticipates for Option 4¹²¹.

234. Furthermore, Ofcom's judgement is inconsistent with its earlier conclusion that handset price and other elements are more important than price variation terms to customers [\$6.17].

Non-price variations

235. Ofcom has not identified any concerns in relation to how the current rules have been applied to any non-price changes. Accordingly, Ofcom proposes to maintain the current rules and proposes that the "material detriment" test should remain in GC9.6 for any non-price variations.
236. We note Ofcom's proposal. We agree. We believe that should Ofcom proceed with option 4, then it must apply the material detriment test in respect of non-subscription prices too.

Implementation of any new regulatory interventions

Implementation Timescales

237. We note Ofcom considers a three month implementation period from the time it issues its Statement should be sufficient to enable Communications Providers to make the necessary changes to their planned advertising/marketing and contractual documentation as well as staff training [\$6.58].
238. It is not clear on what basis Ofcom makes this judgement.
239. We believe 3 months is insufficient. Depending on the outcome, the intervention could result in system changes to ringfence and differentiate tariffs.

¹²¹ Neither does Which?'s website. See earlier comments.

Application to new contracts only

240. We agree with Ofcom's proposal that any new regulatory requirement should only apply to new contracts (ie. Communications Providers should not be required to make changes to existing contracts). [§6.59.]

CONCLUDING COMMENTS

241. We have welcomed the opportunity to comment on Ofcom's preliminary conclusions. As we explain in this response, we have reservations in a number of areas.
242. We are concerned that, contrary to Ofcom's intent, the outcome of its proposed intervention will not benefit customers overall.

Telefónica UK Limited
March 2013

ANNEX 1

Update 2: Price rises in fixed term contracts consultation

Breakdown of consumer complaints to Ofcom about price rises, September 2011-May 2012

Following a request from a stakeholder, we have decided to publish on an anonymised basis a full breakdown of the underlying data to the consumer complaints referred to in paragraphs 2.8 and 4.5 of the consultation document¹. This is in addition to the breakdown of the total number of complaints per category published on 16 January 2013.

The table below provides a breakdown of the 1644 complaints examined by Ofcom about price rises as a “snapshot in time” for the period between **September 2011 and May 2012**:

	TOTAL	Main reason for complaint					
		Amount	Transparency	Unfair	ETC	All	Other
Provider A	1322	214	293	336	149	39	291
Provider B	145	24	60	30	7	3	21
Provider C	67	15	19	18	10	0	5
Provider D	39	8	15	4	0	0	12
Provider E	33	2	7	7	0	0	17 ²
Provider F	26	0	2	10	0	0	14
Provider G	12	3	3	2	0	0	4
TOTAL	1644	266	399	407	166	42	364
% of total	100%	16%	24%	25%	10%	3%	22%

Complaint categories

We categorised the complaints as follows:

- **Amount:** consumers complaining specifically about the amount of the price rise and how it could result in material detriment and/or financial hardship for them.
- **Transparency:** consumers complaining specifically about the lack of transparency of variation terms. These consumers complained about the price rise because they had assumed that the price was “fixed” for the duration of the contract term.
- **Unfair:** consumers complaining specifically about the principle of price rises in fixed term contracts and how they consider it “unfair” that providers can raise prices when they have already agreed to a fixed term contract.
- **ETC (early termination charge):** consumers complaining specifically about the application of the ETC and/or amount of the ETC quoted when they have asked to cancel their contract to avoid the price rise with their provider.
- **All:** consumers complaining about all the above issues.
- **Other:** consumers expressing general dissatisfaction about a price rise.

Limitations of the above complaints data

Stakeholders should note that the number of complaints reported above is the raw data only. As providers vary in size, the above data is not directly comparable between each provider as the complaint numbers have not been recalculated to be presented as the number of complaints as a proportion of subscribers.

¹ <http://stakeholders.ofcom.org.uk/consultations/price-rises-fixed-contracts/>

² This figure includes 10 complaints about the provider's notification process.