Ofcom Consultation on Price Rises in Fixed Term Contracts

Response from Hutchison 3G UK Limited t/a Three

1. Three welcomes the opportunity to respond to Ofcom's consultation on 'Price rises in fixed term contracts.'

2. Three's response is focusing on Ofcom's preferred option (option 4 – modify GC9.6 so that consumers are able to withdraw from a contract without penalty for any increase in 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)).

3. Whilst Three supports the underlying principle behind Ofcom's preferred option that, consumers must be able to make an informed decision when entering into a contract and that any rules must be clear and straightforward and must address the consumer expectation that their monthly recurring charge and inclusive allowances should be fixed for the term of their contract, we believe that:

    a. It is not proportionate for such regulation to apply to all price increases, but should be limited to any increase in the monthly recurring charge or any change in the inclusive allowances which would effectively constitute a (unit) price increase in respect of the inclusive allowances, as this aligns (according to Ofcom's research (from its complaints and Which?'s fixed is fixed campaign)) with the consumer expectation of what will be fixed for the term of their agreement and there are already specific regulations with respect to out of bundle/additional charges; and

    b. Any such regulation should create a level playing field and therefore should apply to all communications industries that Ofcom regulates, not just to Communications Providers who provide Electronic Communications Services, in order to avoid the ability to circumvent the regulation by increasing the price of services which are not regulated by the General Conditions of Entitlement (for example, cable/pay TV service packages).

4. We have set our rationale in respect of these issues in more detail below.

To Whom Should Such Regulation Apply?

5. Firstly, there is a question as to who any regulation in respect of price increases in fixed term contracts should apply. As stated above, Three believes that any regulation with regard to

price rises in fixed term contracts should be clear, straightforward and create more of a level playing field.

6. We note, from the Consultation, that Ofcom is of the view that the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCRs) are complex and their effect is uncertain which has led to difficulties in Ofcom taking enforcement action under those Regulations. We also note that the UTCCRs are not specific to the communications sector but apply to all sectors in respect of potentially unfair terms in consumer contracts.

7. There is a wider policy issue as to whether, if a designated enforcer of the UTCCRs is of the opinion that such Regulations are too complex, uncertain and difficult to enforce then, as those Regulations apply to all sectors who contract with consumers (not just the Communications sector), if there is potential consumer harm arising from interpretation and enforcement difficulties with those Regulations, this should be addressed by Government through legislation, as opposed to through sectoral specific regulation.

8. Putting aside that wider policy issue, we note that Ofcom's preferred option is to amend the General Conditions of Entitlement (specifically GC9) which applies to Communications Providers who provide Electronic Communications Services.

9. Three believes that, in order for any change proposed by Ofcom to be effective, it should apply to all communications services that Ofcom regulates (fixed voice, mobile, broadband and pay TV), in order to prevent the rules being effectively circumvented by providers increasing the price of services which are not regulated by the General Conditions of Entitlement (for example, pay TV service providers). Some providers offer a bundle of services to consumers – (for example, providers may offer their customers pay TV services, as well as broadband and telephony services as part of an overall package of services) – if all of those communications services are not subject to the same rules regarding price increases in fixed term contracts, there is a risk that, for example, a pay TV provider may simply increase the prices of their pay TV contracts in order to circumvent any restriction or regulation in respect of price increases for broadband/telephony services.

Application To All Prices, As Opposed to the Monthly Recurring Charge & Inclusive Allowance

10. Ofcom are proposing, in their preferred option, that consumers should be able to withdraw from a contract without penalty if ANY price is increased, not just a price increase in respect of the monthly recurring charge & inclusive allowance.

11. Whilst Three agree:

a. that mid-contract price increases in respect of the monthly recurring charge are becoming a threat to transparent pricing and to competition, making it harder for consumers to make an informed choice when comparing the monthly recurring charge and inclusive allowance for fixed term contracts; and

b. that Ofcom should take this opportunity to level the playing field and ensure that all Communications Providers price their recurring monthly charges in an open way to provide clarity for consumers so that they can make an informed choice when they make a contract commitment;

12. Three do not agree that consumers should be able to withdraw from a fixed term contract without penalty if the price of ANY service increases as Three believes that this proposal:

    a. is not proportionate, does not appear to align with the consumer expectation and may lead to impacts which would be adverse for consumers and the market generally (such as a risk that consumers will no longer be obtain a device in a way which is affordable or accessible and the possible introduction of two separate agreements for the supply of services and the device will lead to further complexity and confusion for consumers), and

    b. does not align with other regulation/regulatory developments.

<u>Proportionality & Impact on Market</u>

13. The context to this consultation is that the average price of mobile voice calls has fallen by 42% in real terms in the 5 year period from 2006 to 2011, according to data derived from Ofcom's 2012 Communications Market Report. Mobile data charges have also significantly reduced.

14. We note that Ofcom have cited other examples of where other Communications Providers have sought to levy price increases, however, prices increases have not traditionally tended to be a regular occurrence and this appears to be supported by some of the findings presented by Ofcom in the consultation with regard to lack of consumer awareness of the possibility of price increases as it is not a regular occurrence (according to Ofcom, a quarter of consumers complained that they felt they were not made aware of the potential for price rises in what they believe to be "fixed" contracts).

15. Ofcom state that the price the consumer has to pay for the services is one of the most important contractual terms. This is supported by the prominence given (in both advertising and at point of sale (in compliance with GC23)) to the length of the minimum term of a fixed term contract, the monthly recurring charge payable throughout that minimum fixed term and any inclusive allowance the customer receives in return for payment of the monthly recurring charge throughout the minimum fixed term. This also appears to align with both Ofcom's research from complaints it has received - that the customer expectation was that the contract price (i.e. the monthly recurring charge) was fixed for the contract's length and Which?'s fixed is fixed campaign.

16. Three believes that the proposal to fix ALL prices in fixed term contracts, including those where a Communications Provider has no control over or ability to foresee some relevant input costs, (and that is the case with many out of bundle charges) is not supported by the consumer expectation and is not a proportionate response to the issue.

17. Nor would the application of the regulation to any price increase reflect the consumer choice options available to consumers in both instances. In the case of the monthly recurring charge, the consumer has no option but to pay the increase or leave and pay an early termination fee. However in the case of an increase in the out of bundle charges for DQ services, the consumer can choose not to use that service and will not consequently be liable for any payment. As Ofcom is aware, the test of fairness in respect of a potentially term (under UTCCRs) is a term that, contrary to the requirement of good faith, causes a significant imbalance in the parties' rights and obligations under the contract - by bringing out of bundle charges into scope, Ofcom is potentially creating an imbalance in the parties rights under the contract, to the detriment of the Communications Providers

18. However, whilst Communications Providers are able to anticipate some future direct costs, there are other charges, for example, premium rate, non-geographic numbers, roaming charges which can vary significantly and this is generally why such charges are "out of bundle" – i.e. not included within the inclusive allowance of tariffs.

19. The proposed intervention therefore risks a market distortion, particularly in relation to additional charges (such as non-direct debit payment processing fees that may be subject to change by the Banks) and call charges that are not generally included in bundles (e.g. international calls, special rate services, directory inquiries). With respect to call charges for example, the input costs (termination charges) for such charges are generally completely out of the control of the originating operator and not predictable. Often, the charges are levied via a transit operator and so there is no direct relationship between the originating operator and the terminating operator.

20. Unless Ofcom were able to regulate all wholesale rates (both domestic and international), the Communications Providers would be at the mercy of exorbitant wholesale price increases that they could not have forecast or mitigated against and would either have to bear the loss themselves or risk their customers being permitted to leave them with a device, the cost of which cannot then be recovered through subsidisation. This would create a worrying precedent, whereby Ofcom believed it was possible to indirectly regulate wholesale providers via obligations placed on originating providers.

21. Further, the regulation of all wholesale prices would also still not address the issue of other, additional charges, that apply where, for example, a customer chooses to pay via a non-recurring payment (e.g. by cheque or via a manual card payment), Three is subject to wholesale payment processing charges from the banks for administering such payments and, given the significant market power of the banks in the payment processing market, it is not realistic for Communications Providers to mitigate any unilateral increase applied in these wholesale payment processing costs. Ultimately, these costs would have to be passed on to ALL customers if all prices were to be fixed, rather than just those who have actually used those additional services through the choices they have made, which would be more proportionate and fairer approach.

<u>Alignment with Other Regulation/Regulatory Developments</u>

22. As noted, the inclusion of ALL prices in Ofcom's preferred option, as opposed to limiting the ability for customers to be able to withdraw from a contract without penalty if the monthly recurring charge increases and/or the inclusive allowance is changed (decreased), does not seem to take account of, or align with, other regulation/regulatory developments. There is already much regulation (both existing and forthcoming) with respect to out of bundle/additional charges that will provide consumers with substantive protections and, in many cases, militate against prices. Therefore further regulation in respect of these does not seem proportionate. Moreover, Ofcom's proposal does not seem to align with some of these regulatory developments.

    a. *<u>GC23 & Ofcom Guidance on Additional Charges & Other Consumer Laws</u>*

        i. We note that there is already existing regulation both in terms of general consumer law for all sectors (Unfair Terms in Consumer Contract Regulations and Consumer Protection from Unfair Trading Regulations) and specific to the Communications Sector (GC23 and Ofcom Guidance on Additional Charges) in respect of with regard to fairness and transparency, indeed we note that the existing sector specific regulations specifically governs the fairness of terms and charges in respect of consumer communications contracts.

ii. In addition, there is regulation specifically in respect of out of bundles charges.

b. *EU Roaming Regulations – Separate Sale of Regulated Roaming Services Within the EU*

i. As Ofcom is aware, currently all retail roaming services are provided together with domestic services by the domestic Communications Provider. However, EU Regulations have been introduced (Regulation (EU) No 531/2012) , which introduce the concept of the separate sale of regulated retail roaming services if the customer wishes to make that choice, so as to enable a roaming customer to make an informed choice to select an alternative roaming provider for their regulated roaming services. This is based upon:

1. **Transparent information -** being presented to the customer at point of sale which separates information about the services they are agreeing with their domestic Communications Provider, from information about optional/additional services outside not included in their contract with their domestic Communications Provider;

2. **Informed Choice** – the customer can then use this information and, based upon their individual communication service needs, make an informed choice about whether they wish to be supplied with their regulated roaming services by an alternative roaming provider.

ii. This approach from the EU to providing customers with transparent information and choice about additional/optional services which are outside of the core services which they've contracted with their domestic Communications Provider (i.e., monthly recurring charge & inclusive allowance in return for that monthly recurring charge), is not consistent with the approach Ofcom is seeking to take in respect of its preferred option by including increases in ALL prices (even those outside of the price and service (monthly recurring charge & inclusive allowance) which the customer and domestic Communications Provider have agreed).

c. *Non-Geographic Numbers*

i. We note that under Ofcom's review of how to simplify non-geographic numbers, the proposal is that the call cost will be "unbundled" so that consumers will know exactly how much is paid to their Communications Provider and how much is passed on to other companies. The cost would therefore be made up of two parts:

1. An Access Charge (which goes to the Communications Provider connecting the call); and

2. A Service Charge (price, set by the service provider – paid to terminating provider and service provider).

ii. According to Ofcom's stated aims, this will encourage competition and allow service providers to be clear and unambiguous about how much the call to them costs and the cost of connecting such calls.

iii. This "unbundling" recognises that the Communications Providers are not in direct control of all elements of the charge for non-geographic numbers and that, in particular, the Service Charge is not set or controlled by the originating Communications Provider.

iv. The approach taken by Ofcom in respect of non-geographic numbers is to recognise that, some costs are outside of the originating Communications Provider's control and to ensure competition and consumer choice of these optional services through increased transparency of information, thereby permitting effective consumer choice. Three believe a similar, consistent approach should be taken to all out of bundle/additional services.

d. *Recent ASA Adjudication*

i. We note that Ofcom have referenced the recent ASA adjudication (at paragraph 4.56) of the Consultation. Ofcom have noted that the recent ruling by the ASA concerned an advertisement where the consumer had an obligation to pay the monthly price for the duration of a minimum contract period. Ofcom note that the ASA considered that, because the monthly price of the contract was likely to be of significant important to consumers electing to take a fixed term contract, if there was potential for the monthly tariff price to be increased within that fixed term, this should be made clear in the advertising.

ii. Two key points arise from this adjudication:

1. Firstly, the ASA took the view that, where consumers elected to take a fixed minimum term contract, the consumer expectation was that the monthly recurring price was of significant importance and the consumer expectation was that this would be fixed for the minimum term of the contract (unless stated otherwise in the advertising). This also seems to align with both Ofcom's research from complaints it has received - that the customer expectation was that the contract price (i.e. the monthly recurring charge) was fixed for the contract's length and Which?'s fixed is fixed campaign.

2. Secondly, the ASA clearly took the view that increased transparency would ensure an effective and informed consumer choice could be made. This approach would seem to align with existing regulation from Ofcom in the form of GC23, whereby, transparency at point of sale, is mandated to assist consumers in making an informed decision and Three believe that transparency of out of bundle/additional charges is the appropriate and proportionate approach to assisting consumers in making an informed choice regarding any out of bundle or additional services they may elect to use outside of any inclusive allowance for which they are paying their monthly recurring charge.

iii. As such, Three believe this supports the premise, that whilst the consumer expectation is that the monthly recurring charge (and inclusive allowance) will fixed during the minimum term of their contract, charges for other services the consumer may choose to use may not be fixed and that, provided there is transparent information relating to those charges that may be subject to change and the consumer is given a fair opportunity to review those charges (in accordance with the transparency requirements set out in GC23), the consumer is then able to make an informed choice about whether to use those services that are outside of bundle/are for additional services.

<u>Impact on Consumers & Market Generally</u>

23. Three notes that Ofcom has made reference to consumer harm as justification for the proposed intervention and had made a number of assertions as to the economic impact from their proposals, however, we also note that Ofcom has not carried out an impact assessment that considers all possible impacts from the proposed intervention.

24. Three believes that the inclusion of ALL prices in Ofcom's preferred option, as opposed to limiting the ability for customers to be able to withdraw from a contract without penalty if the monthly recurring charge increases and/or the inclusive allowance is changed, may have some adverse impacts on consumers.

25. Three believe that there is a risk that if customers are permitted to withdraw without penalty if ANY price increases, there is a real risk that consumers will no longer be able to access free (or subsidised) devices as a result, as Communications Provider will not be able to bear the risk of all customers being permitted to leave them with a device, the cost of which cannot then be recovered through subsidisation. The absence of such contracts from the market could be very detrimental to consumers who use such contracts to go on-line (as envisaged by the Government's "Digital Britain" vision) with little or no investment.

26. Ultimately, either:

    a. these costs would have to be passed on to ALL customers if all prices were to be fixed, rather than just those who have elected to use those additional services which are subject to a price increase - it does not seem a proportionate and fair approach that all customers should have to bear the increased costs passed through for services which are only used by some customers; or

    b. the device would need to be either purchased upfront by customers or customers would need to enter into a separate financing agreement with a credit institution if they wished to spread the cost of paying for the device. This option has two main issues:

        i. Firstly, Ofcom note that a perceived lack of transparency and confusion have led to some of the consumer harm that Ofcom perceive exists. However:

            1. as smart devices carry a significant upfront cost which most consumers do not wish to pay upfront, there has been an increase in the number of consumers electing to take 24 month contracts which allow customers to obtain the device and services they want at a monthly price that is affordable to them (the increase in 24 month minimum term contracts is specifically noted by Ofcom in its consultation);

            2. if consumers had to enter into a separate financing agreement for the supply of the device, this would only seem to serve to increase the complexity and confusion for customers.

ii. It would also lead to a number of practical, operational challenges for the Communications Providers (for example, the consumer contract terms would need to be amended to reflect this change, there would also need to be changes to the systems that produce the point of sales (GC23 mandated) information, training of all sales staff (with the impact on sales efficiency due to the increased time during sales to explain the separate financing agreement for the device to the customer)). This would also mean, from a practical perspective, that a three (3) month implementation period following the publication of a statement by Ofcom would not be sufficient to implement all of the changes needed.

iii. It could also mean that some consumers may not be able to obtain the smart device (that can use all services, including enabling the consumer to get online) as they may find they are "financially excluded" due to their financial background as against the level of risk that a credit institution may be prepared to take when assessing their credit worthiness. This may impact certain consumer groups (for example, vulnerable groups) more than others.

c. In summary, although Three believe this supports the premise, that whilst the consumer expectation is that the monthly recurring charge (and inclusive allowance) will be fixed during the minimum term of their contract, charges for other services the consumer may choose to use may not be fixed and that, provided there is transparent information relating to those charges that may be subject to change and the consumer is given a fair opportunity to review those charges (in accordance with the transparency requirements set out in GC23), the consumer is then able to make an informed choice about whether to use those services that are outside of bundle/are for additional services.

Conclusion

27. Whilst Three supports the underlying principle behind Ofcom's preferred option that any rules must be clear and straightforward and must address the consumer expectation that their monthly recurring charge and inclusive allowances should be fixed for the term of their contract, we believe that it is not proportionate for such regulation to apply to all price increases, but should be limited to any increase in the monthly recurring charge or any change in the inclusive allowances. On that basis, we would ask that Ofcom reconsider the scope of their preferred option and take account of the real concerns raised by Three, particularly in relation to consumer detriment around the choice and availability of subsidised handsets.