Price rises in fixed term contracts – uSwitch.com response

uSwitch.com has been helping consumers to make informed decisions regarding utility suppliers, including the communications market, for more than ten years. By ensuring that consumers are educated and engaged, we help them to get the best value deals for their individual needs and save money on their household bills.

In a tough economic climate successful budgeting is vital to many consumers. Being aware of any variable costs and how bills may increase are the first steps in helping consumers achieve this. It's also important that consumers are able to act, where possible, to avoid price rises. Therefore we welcome Ofcom's investigation into price rises in fixed term contracts, and hope that steps can be taken to ensure consumers are protected as much as possible, while maintaining a competitive market.

Consumer harm

We agree that, with household expenses rising and many consumers on a tight budget, unexpected increases to a cost that consumers expect to be a constant, can cause harm. Consumers can also be impacted by providers' ability to implement price rises without the automatic right for consumers to terminate the contract without a penalty. It's important that consumers are sheltered from surprise increases to their household bills wherever possible, or at least given a call to action to avoid such increases.

We also agree that consumers are currently harmed by the inconsistent application of the 'material detriment' test. We feel that increased transparency over this would help a number of consumers – especially vulnerable ones - negate the effects of a price rise. Also, the current state of allowing providers to determine what constitutes harm isn't in the best interest of the consumer. We believe that Ofcom should provide guidance as to the definition of material detriment. However, implementing Option 4 would make this clause redundant in the Telecoms market, which would help increase clarity and reduce confusion.

Risk

In terms of where pricing risk should lie, we agree that because providers are best placed at predicting the costs involved over the life of a contract, they should take a bigger share of it. If providers are forced to increase prices due to poor forecasting, they should take the financial consequences, not their customers. Therefore, they should give customers a way to avoid any increases to their monthly bills.

However, enforcing them to refrain from implementing price rises could lead to them increasing initial costs in order to cover the possibility of unforeseen increases they didn't predict at the outset of the contract. In other markets consumers tend to pay a premium for the peace of mind of a truly fixed contract. In the energy market we have seen this premium decrease, and we would hope that the competitive nature of the Telecoms market would lead to downward pricing on any fixed price premium. However, it is important to note that in the energy market this took several years.

In regards to which prices networks should be able to predict, we agree with Ofcom that all rises – including those to non-geographical numbers - should trigger the release clause as proposed by Option 4. The only exception should be increases due to VAT. However, we would therefore expect any VAT reduction to be passed on to customers too.

Clarity and transparency

Our own research suggests that providers aren't clear enough about the possibility of price variation in a fixed-term contract. Although contracts state that prices are variable, many consumers aren't aware that this is the case – from our research, 61% of consumers believe that a fixed term contract means a fixed price. This lack of transparency causes consumers harm, as they are often unprepared for the cost of their contract increasing.

In the energy and mortgage markets, a contract with a fixed price is clearly referred to as a fixed price deal. If Option 4 isn't implemented, it's vital that Ofcom ensures that the possibility of price variance is made clear at the POS – and issue fines when a provider is judged to be mis-leading consumers.

In the further interests of clarity, if Option 4 isn't implemented, when providers increase prices every customer affected should receive a communication in their preferred format – namely email or post. When Orange sent texts to inform of price rises there was a consumer backlash – this was a lot to do with the medium as well as the message. We feel that this letter should be based on a template that Ofcom draws up thus ensuring uniformity and clarity within each part of the telecommunications market.

We also believe that when a consumer receives a notification about a price rise they should be made aware of what their new bills will be, a reminder of how long is left on their contract and the options open to them, referring to GC6.9 – and Ofcom's guidance as to what this entails.

If Option 4 is implemented, providers must be obliged to communicate that consumers are able to leave. We feel that a month is a suitable window for consumers to act within. This is the window energy customers have to notify their supplier that they are leaving, and our research shows that a third of consumers (34%) feel a month is fair.

We recognise that the Telecoms market does not currently offer consumers sufficient protection. Along with a lack of education, many consumers come to harm regarding price increases. With this in mind, we have examined and appraised Ofcom's proposals:

Option 1

We agree with Ofcom's recognition that price rises in fixed term contracts have a negative impact on consumers and their finances, and that something needs to be done. Our own research shows that consumers are confused by pricing, harmed by price rises and that the market is lacking transparency. Therefore we agree with Ofcom that Option 1 isn't viable.

Option 2

We agree that this option is necessary, but not sufficient. Ofcom should publish guidance on the application of GC9.6 and the UTCCRs to price rises and relevant contracts. This guidance would increase transparency, give consumers consistency across suppliers and ensure that they are protected from being at the whim of the providers.

However, guidance alone wouldn't suffice. Consumers must be able to respond to price rises so that they can avoid them, or at least minimise the effects - especially in a difficult economic climate. Enabling consumers to act to negate the effects of price rises would also hopefully encourage less apathy and more engagement. But ultimately, the successful implementation of Option 4 would mean that consumers wouldn't need this guidance, as GC9.6 would become redundant.

Option 3

This option would clearly define fixed price and fixed term contracts – removing questions about clarity of price variation. Everything Everywhere (EE) has recently pledged to be more transparent about the variable nature of current plans at the POS – while highlighting a fixed option. We feel that highlighting that one plan is fixed in price goes some way to clarifying that the other plan is not.

However, having a two-tiered pricing system for mobiles and broadband could add to the complexity of the market, and create less engaged consumers. In fact, in the energy market, restrictions on the number of tariffs each supplier can offer are about to be brought in to reduce complexity and customer confusion.

We also fear that a two-tiered pricing system could lead to a large premium for fixed price plans as providers would have to protect themselves from any possible price rises. We have already seen those customers opting to fix the price of their EE contract face a premium.

The premium starts at 50p, which is reassuring. suggesting that the price of fixing perhaps wouldn't be as high as we were worried about. However, it has set a precedent for fixed plans costing more than variable and for their premium to cost more than the average price increase.

Analysis of the EE premium shows that customers paying £10, £10.50, £20.50, £41 or £61 a month would be better off if there were annual increases of 3.33% (the most recent increase) for both years of a two-year contract. However, the majority of T-Mobile and Orange plans would leave consumers who fix worse off. In fact, those on a £35 monthly contract would need to see annual increases of 3.76% each year of their contract to be better off paying a premium to fix.

Our other concern about this option is regarding the automatic opt-in. This is especially true if fixed price plans do carry a premium as consumers who aren't aware of the automatic opt-in could end up on a more expensive deal, even though they may be prepared to take a gamble for a lower monthly bill.

Those who are aware, and would rather take the risk, could opt-in to a cheaper variable tariff, but would lose any protection against price rises by doing so. We also worry that providers may increase prices for those on a fixed-term variable contract to balance the increased costs of customers on fixed-price plans, and also because consumers who have opted-in to a variable contract would have no protection.

If this option was considered, Ofcom would have to work with stakeholders to educate consumers. However, we don't feel that consumer education is the answer for all, and as discussed below, making all contracts fixed-price would remove this doubt altogether.

Option 4

This option certainly goes the furthest in protecting consumers and would ideally lead to an end of mid-contract price rises – which would be hugely beneficial to consumers trying to budget their finances. Our own research shows that over three quarters of consumers (76%) support this option.

We have already seen Tesco Mobile commit to not increasing prices for customers during the life of their contract. This supports our belief that providers are well positioned to predict the cost of a contract for its life, factoring in any possible price rises they may face and the cost of a handset, when setting the cost of a contract. Consumers who sign up to a Tesco Mobile deal will have the ultimate protection for the life of their contract. Although Tesco Mobile is a smaller provider, we still believe it is possible for other networks to follow this lead.

If this action doesn't stop providers increasing prices, at least with this option consumers would have the right to act. In other markets, namely energy, consumers are able to avoid a price rise by switching provider without incurring exit fees. This helps to protect consumers and helps to encourage a competitive market and consumer engagement. Our research reveals that if consumers were able to switch their telecoms provider without exit fees following a price rise, 47% would be more likely to shop around for a better deal, and 37% would be more likely to switch to a better deal.

However, we do have concerns with this option. If providers were unable to implement a price rise for the length of a contract – 24 months in most mobile contracts – we could see monthly prices, or upfront fees, increase in order to offer a safety net for providers who may have to swallow increases to their costs over this time.

The longer the contract, the more likely and higher these increases could be. As the vast majority of mobile phone deals on the market are 24 months, we feel this problem is more pressing in the mobile sector.

To support this concern further, as previously mentioned, Everything Everywhere has introduced a range of fixed tariffs which have a price premium. If Ofcom was to enforce that all plans were fixed, we fear that EE would simply remove its variable plans, leaving its more expensive deals as the only option for consumers.

We could also see consumers roll on to more expensive plans as soon as they're out of contract. Providers would be able to increase prices once a contract has finished. Although some consumers would move providers or plans, or negotiate a better retention deal, many consumers remain unaware that their contract has finished – and that they would be liable to a price increase. This is a bigger problem in the broadband market where a third of consumers haven't switched provider for 3 years, and half have never switched.

Therefore, we would expect Ofcom to take the opportunity to further increase clarity and transparency in the mobile market by ensuring that networks issue a letter to customers before the end of their contract, stating the price of the deal that they would be moved onto. This happens in the energy industry (most customers are given a two month warning) and we believe there is no reason for it to not happen in the Telecoms market.

It would give consumers greater transparency as well as the information they need to make an informed decision and to shop around, meaning that hopefully more consumers make the competitive market work for them.

We also have concerns about how Option 4 would work in practise, based on learnings from the energy market. Here, a clause enabling customers to leave a variable price contract mid-term without exit fees in the case of a price rise, does not lead to suppliers holding off from increasing prices.

If this action didn't act as a deterrent for mid-contract price rises, there would be complications because of the hardware involved in many Telecoms contracts, such as a mobile handset or broadband router. Would customers have to return these? Would insurance become mandatory to ensure that handsets are in good condition in case they get returned? Just 39% of consumers would be happy to return their handset if they left mid-contract following a price rise. We fear that this could lead to the end of free mobile handsets, free routers and installation in broadband, which would in turn penalise those customers who can't afford upfront costs.

The broadband and fixed line market also opens up a number of complications considering the growing trend in bundling. If a customer has home phone, broadband and digital TV from a provider that puts up its line rental, will a consumer break up a bundle and just switch their home phone? And what about their broadband? It's unlikely that a customer would switch one element. For providers like Virgin, who offer quad-play bundles, this is even more complicated. Would providers not be put off implementing price rises because of the hassle involved in breaking a bundle, or would consumers be able to leave the whole bundle if one element increased in price?

We are delighted that Ofcom has already demonstrated such a firm grasp of the need for change, and hope that consumer protection can be increased while ensuring a competitive market. We believe that the level of protection consumers need would be best provided by Option 4. However, we have a few areas of concern, and welcome any feedback on our questions as to how it would work in practise, especially in light of the popularity of the bundles market.