**Ofcom statement on Additional Charges (updated Guidance)**

## Introduction

1. In December 2008 Ofcom published our *Guidance on unfair terms in contracts for communications services* ("the *Guidance*").

2. The *Guidance* set out:

   2.1 how Ofcom considers The Unfair Terms in Consumer Contracts Regulations 1999 ("the Regulations") are likely to apply to certain standard terms in contracts for communications services; and

   2.2 in particular, our view on terms we think may be unfair (or potentially unfair).

3. The *Guidance* focused on contract terms which provide for the payment by the consumer of additional charges, default charges, minimum contract periods and minimum notice periods.

4. There have been two key developments since we published the *Guidance:*

   4.1 in November 2009, the Supreme Court gave its judgment in the Office of Fair Trading's challenge to contract terms providing for unauthorised bank and building society overdraft charges;[1] and

   4.2 Ofcom have been engaged in an enforcement programme (which has resulted in BT, TalkTalk and Virgin Media agreeing to change their terms and reduce their charges relating to *early termination charges*[2] for fixed voice and broadband services).[3]

   This statement is about how we have updated the *Guidance* in light of these developments.[4]

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[1] *Office of Fair Trading v Abbey National plc and others* [2009] 3 W.L.R. 1215
[2] The charges consumers often face for ending their contract before the end of a fixed minimum period.
[3] See http://www.ofcom.org.uk/consumer/2010/06/cheaper-charges-for-uk-consumers-to-end-phone-contracts/
[4] Though neither this statement nor the *Guidance* are an exhaustive statement about the application of the Regulations to terms in contracts for communications services. What the *Guidance* says about its status (for example, in its paragraphs 7 – 9) is also relevant to this statement.

## Summary

5. Ofcom's view is that the Supreme Court's judgment has only a limited impact on the *Guidance*.

6. The judgment only concerns the scope of one part of an exemption from the Regulations' fairness requirement for certain contract terms (in this statement we call this "the exemption"). The judgment does not concern, for example, what the Regulations' fairness requirement means, and so does not affect Ofcom's view on that. And, in Ofcom's view, the Supreme Court's approach to the exemption was not substantially different in principle to that we took in the *Guidance*.

7. In particular, the Supreme Court confirmed that the exemption covers the *quid pro quo* consumers make with suppliers: what they are buying and the price they pay for it. The Regulations do not regulate whether the price consumers pay in exchange for goods and services is appropriate: too high or good value for money. Neither did Ofcom suggest that in the *Guidance*.

8. The judgment gives guidance on what constitutes the price for goods and services within the exemption. We agree this will mean some charges covered by the *Guidance* – like *itemised* and *paper billing charges* – may be within the exemption. But, it remains the case, in Ofcom's view, that many will not, and the judgment has little or no impact on the overall views Ofcom expressed about them in the *Guidance*.

9. Most importantly, since we published the *Guidance*, our enforcement programme has focused on terms providing for *early termination charges*. These are the additional charges about which Ofcom continues to receive the most consumer complaints, and where consumer detriment is high. The judgment is clear, in our view, that these terms (and charges) are outside the exemption and must be fair,[5] as we said in the *Guidance*. So, our position in respect of *early termination charges* is unaffected by the judgment and we are

[5] And will be unfair if the charges they provide for are too high.

continuing to focus our enforcement priority on these charges on the basis set out in the *Guidance*.[6]

10. This means we have made limited changes to the *Guidance* as a result of the judgment. We have also made some other changes to clarify and simplify the *Guidance*, especially in light of our experience of applying our view of the law to *early termination charges* in the fixed voice and broadband sectors.

**The Regulations and relevant terms and charges**

11. The Regulations say that standard form terms and conditions in contracts between suppliers (here, communications providers ('CPs')) and consumers must be fair. They set out the fairness test that applies. A limited number of terms, however, are wholly or partially exempt from this fairness requirement.

12. The exemption, in Regulation 6(2), says:

"*(2) In so far as it is in plain intelligible language, the assessment of fairness of a term shall not relate—*

*(a) to the definition of the main subject matter of the contract, or*

*(b) to the adequacy of the price or remuneration, as against the goods or services supplied in exchange*."

13. In the *Guidance* we set out our view of:

13.1 whether each of the relevant terms and charges is subject to the fairness requirement or falls within the exemption from it; and

13.2 if the fairness requirement applies, how.

14. The terms and charges covered by the *Guidance* are:

14.1 *non-direct debit charges*: charges CPs impose on consumers who pay their bills by means other than direct debit;

[6] We have amended the Guidance accordingly. But, the absence of an indication of priority in relation to a particular type of term does not mean Ofcom will not undertake investigation and enforcement work in that area. We reserve the right to do so, and any CP using any term we consider unfair is liable to action.

14.2 *itemised* and *paper billing charges*: extra charges for receiving hard copy and/or itemised bills;

14.3 *default charges*: charges for late payment, payment failure and reconnection;

14.4 *initial minimum contract periods* and *early termination charges*: terms providing for contracts to be of a fixed minimum period and terms charging consumers for terminating them before the end of that period;

14.5 *subsequent minimum contract periods*: terms imposing further fixed minimum contract periods where certain events occur;

14.6 *minimum notice periods*: terms requiring consumers to give minimum periods of notice to end their contracts; and

14.7 *cease charges*: terms requiring consumers to pay a charge to stop receiving a service even outside any fixed minimum contract period.

15. Our view was that the fairness requirement applies, or could apply, to *non-direct debit charges*, *itemised* and *paper billing charges*, *default charges*, *early termination charges*, *subsequent minimum contract periods*, *minimum notice periods* and *cease charges*. We also considered that *initial minimum contract periods* will usually fall within the exemption.

**Our approach**

*Exempt terms*

16. Our view of the Regulations, in principle, was this. That, as long as the relevant terms are clear and transparent enough, the *quid pro quo* in a consumer contract – what the CP is to sell or supply and what the consumer is to pay for it – is within the exemption. It is not subject to the Regulations' fairness requirement.

17. Put another way, as long as the terms are clear enough that consumers can make informed choices about them, these matters should be regulated by competition and negotiation, not legislation. The law does not step in and require that CPs charge consumers a fair retail price for, say, a phone or broadband subscription. That is for the CP and the consumer to agree. We applied this approach in principle in the *Guidance*.

18. So, for example, we said *paper billing charges* could be within the exemption. They would be if the relevant terms were presented so clearly and transparently that the typical consumer would regard them as part of the price he is paying for what he is buying (and not as a separate, incidental charge).

*Non-exempt terms*

19. But, we also took the view that, where terms are not so clear and transparent, and/or they are not part of the *quid pro quo* described above, they must be fair under the Regulations. Our view was that the law should re-balance inequalities between consumers and CPs. In particular, to stop CPs using terms that confer advantages on them, and/or impose burdens and liabilities on consumers, that would not arise under general law if the term did not exist.

20. So, for example, we said *default charges* and *early termination charges* must be fair. They are not a price, or part of the price, for what the CP supplies under the contract. They are charges levied when the consumer does something he should not (or fails to do something he should). They are incidental or ancillary to, not part of, the relevant *quid pro quo*.

**The Supreme Court's judgment**

21. The key point about the Supreme Court's judgment, in our view, is this. What is exempt from the requirement to be fair is the *quid pro quo* consumers make with CPs. Terms and charges outside that must be fair.

*The exemption*

22. The Supreme Court confirmed that the two parts of the Regulations' exemption from the fairness requirement:

> ' ….. *reflect (but in slightly different ways) the two sides (or quid pro quo) of any consumer contract, that is (a) what it is that the trader is to sell or supply and (b) what it is that the consumer is to pay for what he gets. The definition of the former is not to be reviewed in point of fairness, nor is the "adequacy" (appropriateness) of the latter*.'[7]

23. The Court considered what payments constitute the price that the consumer is to pay for what he gets. Where they are part of that price, they are within the exemption.

24. The Court said identifying, '… *the price or remuneration …. is a matter of objective interpretation* …..'[8] And that:

> '…… *If it is possible to identify such price or remuneration as being paid in exchange for services, even if the services are fringe or optional extras, reg 6(2) will preclude an attack on the price or remuneration in question if it is based on the contention that it was excessive by comparison with the services for which it was exchanged* ….'[9]

25. In other words, any payment that can be identified on an objective basis as the price paid in exchange for goods or services, or as part of the price paid in exchange for a package of goods or services (or part of the package), is within the exemption.[10]

*Effect of the exemption*

26. The Court also considered the effect of the exemption. As the second quote in paragraph 24 above indicates, it means the fairness requirement does not apply so as to demand that the price consumers pay in exchange for goods

[7] Lord Walker at paragraph 31
[8] Lord Mance at paragraph 113
[9] Lord Philips at paragraph 78
[10] See Lord Philips' further comments at paragraph 78

and services is appropriate (not too high). The law does not ask the 'value for money' question: is '£X too much to pay for Y?' That exchange need not be fair and there need not be value for money.

27. Instead, the Court said, the law only requires that the terms about the price be clear and transparent. As long as they are, a consumer is capable of identifying the price and deciding whether to pay it. That is the protection the consumer has in relation to the price.

*Non-exempt payments*

28. The Court also said, however, that not every charge or payment under a contract is part of the price and within the exemption:

> '*This House's decision in the First National Bank case shows that not every term that is in some way linked to monetary consideration falls within reg 6(2)(b)……*'[11]
>
> ' …… *There can be payments which do not constitute either "price or remuneration" of goods or services supplied in exchange*…. '[12] and
>
> '…. *A contract may of course require ancillary payments to be made which are not part of the price or remuneration for goods or services to be supplied under its terms. The First National Bank and Bairstow Eves cases illustrate the distinction by reference to default terms*.'[13]

29. Even payments that are part of the price are subject to the fairness requirement in some respects. The exemption only covers the value for money for question referred to above. In other words, it is not so much whole (price) terms that are exempt from the fairness requirement, only certain limited matters.

30. So, even price payments[14] can be challenged as unfair on grounds other than whether they are too high for the goods and services supplied in exchange:

[11] Lord Walker at paragraph 43
[12] Lord Mance at paragraph 101
[13] Lord Mance at paragraph 113
[14] The terms providing for those payments

'*Further, payments which do constitute price or remuneration in this sense can be challenged as unfair on grounds which do not relate to their appropriateness in amount as against the goods or services supplied in exchange*.'[15]

Other payments under a contract can also be challenged on such grounds.

31. The Court gave examples of the kinds of payments that fall outside the exemption.[16] It referred to payments made under the terms set out in paragraphs 1(d), (e), (f) and (l) of Schedule 2 to the Regulations.[17] These include, in paragraph 1(e), terms which have the aim or effect of, ' …. *requiring any consumer who fails to fulfil his obligation to pay a disproportionately high sum in compensation*.'

32. It also referred[18] to charges payable for breach of contract ('default charges') and what might be called 'quasi-default' charges. That is, charges payable on what would be some sort of default were the relevant term not drafted so as to avoid a breach of contract arising.

**Effect on the *Guidance* (and our enforcement programme)**

33. The approach Ofcom took in our *Guidance* is, therefore, consistent in principle with the Court's judgment. Both make clear that what falls within the exemption from the Regulations' fairness requirement is the *quid pro quo* - again, what the CP supplies and the price the consumer pays for it - under the relevant contract. As long as that is clear, so consumers can make informed choices, the fairness requirement does not apply to it. That is what we said in the *Guidance* and the judgment does not change that.

34. But, the Court confirmed that the scope of the exempt 'price' – that is part of the relevant *quid pro quo* – is wider in some ways than we set out in the *Guidance*.

[15] Again, Lord Mance at paragraph 101
[16] See Lord Walker's further comments at paragraph 43, Lord Philips's at paragraph 83 and Lord Mance's at paragraph 101
[17] Which sets out a non-exhaustive list of terms that may be unfair under the Regulations.
[18] Again, in paragraphs 43, 83 and 101

35. So, the judgment means *non-direct debit charges* and *itemised* and *paper billing charges* are likely to be part of the price within the exemption in many cases, provided they are clear and transparent. It will depend on the precise terms and circumstances in each case, but these charges are fully capable of being (and often will be) part of the price for the package of services a CP provides under the relevant contract. We have amended the *Guidance* on this point.

36. In other respects, we think the judgment confirms the position Ofcom took in the *Guidance*. Most important, given the focus of our enforcement programme, the judgment supports the view that *default charges* and *early termination charges*[19] are outside the exemption and must be fair.

*Early termination and other unaffected charges*

37. An *early termination charge* is not part of the exempt *quid pro quo*. There is a, usually monthly, retail price that falls within that. By contrast, an *early termination charge* is a separate, ancillary payment, payable if the consumer does not meet an obligation to continue a contract for a fixed period. Considered on an objective basis it is quite distinct from the exempt price, for reasons including the following.

38. An *early termination charge* is not paid in exchange for the package of goods and services under the contract. The opposite applies: it is paid when goods and services stop being supplied (because the consumer has ended the contract early). It is paid as compensation for ending the contract early (as opposed to the goods and services).

39. And, applying the fairness requirement to a compensatory payment like an *early termination charge* does not involve asking the value for money question: 'is £X too high a price in exchange for Y goods and services?' Instead, it asks, 'is £X too high as compensation for the consumer ending the contract early?' The exemption precludes the former. It does not apply to the latter. The fairness requirement does.

[19] As well as 'cease' charges.

40. Put another way, applying the fairness requirement to an *early termination charge* does not concern an exempt matter: the appropriateness (adequacy) of the price a consumer pays in exchange for communications goods and services. It would ensure only that the compensation payable when a contract ends early is not excessive.

41. Moreover, an *early termination charge* is payable under a term that potentially falls within paragraph 1(e) of Schedule 2 to the Regulations. That is, one that may be unfair if it requires the consumer to pay a disproportionately high sum as compensation for failing to fulfil an obligation. The Supreme Court expressly identified such payments as falling outside the exemption.

42. It does not matter that an *early termination charge* is payable where the consumer terminates the contract in a way that does not breach the contract. The consumer's early termination is still of the nature of a default: a failure to do what he contracted to do. An *early termination charge* is an example of where the Supreme Court said a supplier:

> '….. *could not convert what were in effect penalties into "price" simply by wording their contracts so as to ensure that the contingencies that triggered liability to pay the charges did not constitute breaches of contract*.'

43. Each of these points underlines the distinction between price payments due in exchange for the communications goods and services under the relevant contract and the payments due on the (quasi-) default of early termination. This distinction was the basis on which Ofcom engaged with BT, TalkTalk and Virgin Media about their *early termination charges* for fixed voice and broadband (see above). It is also reflected in what we say in the Guidance, which remains substantively the same on this point. And, it is the basis on which Ofcom will continue to engage with other CPs in the same and other sectors.

44. The position is clearer still in relation to *default charges*, like *late payment* and *payment failure charges*, which are payable where a breach of contract has occurred. They are another example of charges payable under terms potentially falling within paragraph 1(e) of Schedule 2 to the Regulations. The

Supreme Court expressly contemplates that these sorts of *default charges* are not within the exemption and must be fair.

45. In addition, the judgment does not affect at all the way the fairness test applies to *early termination charges* (or *default charges*). Ofcom's position in the Guidance on *early termination charges* is reflected in the agreements given by BT, TalkTalk and Virgin Media. That position is also substantively unchanged (as is that on *default charges*). We have made only small amendments to the relevant section of the Guidance, to clarify certain points. We will continue our enforcement programme in relation to *early termination charges* as a matter of priority.

*Other terms*

46. As to the other terms covered by the *Guidance* – initial and subsequent minimum contract periods and minimum notice periods – the overall position in the *Guidance* is not changed by the Supreme Court's judgment.

47. The judgment is concerned with part (b) of the exemption about payments that might be part of the exempt 'price.' Terms about the length of contracts and notice periods do not involve the payment of any price. If anywhere, they would fall within part (a) of the exemption relating to the main subject matter of the contract. The judgment refers only briefly to this part of the exemption.

48. As far as the judgment contains comments that might be applied to part (a) of the exemption, we have taken these into account and made some amendments to the Guidance. But, the overall position in the *Guidance* remains the same.