Consultation response – Helping consumers to get better deals in communications markets: Mobile Handsets

We have reviewed Ofcom's consultation in relation to helping consumers to get better deals in communications markets. We have noted Ofcom's intention to limit split contracts to a maximum of 24 months, and the proposed implementation date of early 2020.

Ofcom's key concerns in relation to split contracts are that they:

- Could tie customers into excessively long contracts;
- Inhibit switching; and
- Deny customers the benefits of competition.

Excessively Long Contracts

As Ofcom is aware from conversations with us last year, the airtime on our split contracts is capped at 24 months, in line with the EU Directive and the General Conditions. Ofcom's reference in the consultation to "excessively long contracts" we assume refers to device credit agreements of up to 36 months. In our case, it is the handset agreement which has determined this duration. As we have made clear on a number of occasions, our reasons for including the option of a 30 or 36 month handset credit agreement is to ensure that a larger proportion of the market has access to these handsets; thus increasing competition in the marketplace. Handsets are becoming increasingly more expensive and therefore to meet customer needs and expectations we provide a breadth of choice in relation to the term for both their airtime contracts and handset credit agreements. Notably, for handset credit agreement terms, the majority of our customers are opting for 30 and 36 month terms, by choice.

Ofcom's suggestion is that customers should be able to end their airtime contracts and move to competitors whilst leaving the credit agreement with the incumbent provider. It is our view that this would be confusing for customers who despite separating their handset and airtime contracts for reasons of choice, value only having one combined bill to pay. In addition, Ofcom has not considered the impact of its proposal and the very real possibility that the market would see an increase in credit agreement defaults and an increase in bad debt. Such negative impacts would affect provider strategy and could lead to increased consumer costs, requirement for deposits, upfront payments or increased APR percentages. None of which would be in the consumers benefit.

Switching

Ofcom notes the growing popularity of split contracts among consumers. The benefit to the consumer is that they have increased choice and flexibility when it comes to deciding the period over which they would like to repay the credit they have used to buy the handset under their credit agreement. This enables them to choose how to fund their mobile phone contract over a period that is right for them. This is particularly important at a time when devices are becoming increasingly expensive and have a longer use lifecycle before becoming outdated in form or technical performance and is something our customers tell us they want.

We agree that a customer should be able to switch with ease. However, it is not the case that all customers will get a better deal by switching. The majority of Ofcom's argument in the consultation is that barriers to switching cause harm to the consumer. However, no credit is given to the customer making an informed decision through choice including brand loyalty.

Ofcom commentary sets out views from previous respondents claiming split contracts tie people to long airtime contracts. We disagree that tying people to long contracts is detrimental or likely to cause harm. A longer credit agreement offers certainty and a clear and manageable repayment scheme enabling customers to budget and pay for the handset they want. We ensure that these details are made clear to the customer at the outset. The customer is making an informed decision about how long they want to enter into the device credit agreement with us. We currently offer this on 0% APR basis meaning that it is extremely cost effective way of purchasing an expensive commodity. It is correct that we require customers to fully repay the credit agreement if they choose to move to another provider. This is the basis behind the majority of credit offerings and is certainly not restricted to the telecommunications sector. We are confident that the customer is making this choice fully aware of the length of the agreement and conditions upon which we offer the credit. As stated previously, despite offering varying handset contract lengths customers are choosing longer contract lengths.

The reference to the lump sum payable being a disincentive to switching is not substantiated in any detail in Ofcom's consultation, nor does it provide any evidence of harm to the customer. We know from reviewing customer behaviour that there is a well developed re-sale market for phones, as well as trade-in programmes which enable customers to sell their phone in order to release the value which they could use to pay off their account prior to beginning a new contract with another provider if they choose to.

In our experience, switching becomes more important to customers when they are unhappy with their provider or are unhappy with their handset or airtime. In these instances they want to be able to leave as soon as possible. However, Ofcom's impact assessment does not look to have taken into consideration instances where customers are happy with a provider, they want to stay e.g. brand loyalty, provider relationship, trust in provider). Whilst Ofcom has considered the impact on switching in its consultation, it has failed to provide evidence of the harm suffered by consumers as a result and this not least because 36 month terms are so new to the market that and there is not enough information to accurately gauge whether there is detriment. The majority of our 36 month contracts will not expire until 2020 which means that there cannot not have been a full review of the impact on consumers.

Competition

Ofcom also maintains that by affecting switching, it undermines the competitive process. The mobile sector has never been more competitive than it is today. We have four MNO's, numerous sub-brands such as giff gaff, Voxi, Smarti, countless MVNO's including Tesco Mobile Limited, Virgin, Sky and indirect competitors such as Mobile Phones Direct and Dixons Carphone. The choice available to consumers is broad, varied and certainly competitive allowing customers a huge amount of choice. Choice about how they pay for their phone, when they pay, how they take the services, whether they want a handset as part of the deal, or to pay separately. They get to choose which handset they want. They get to choose how long they want to pay off their handset. Consumer credit is not a new phenomenon for customers, and consumers are increasingly sophisticated. They are aware that they are signing up to paying off their handset over a 3 year period. Customers can do their research and work out the best option for them and then, rather than being tied to a provider, can decide how long they want to sign up with a provider for. Buying a mobile phone is not a passive act; the consumer is making the choices. Since launching Anytime upgrade flex, customers have been actively choosing longer length contracts – our most popular handset contract length is 30/36 months. Customers are well informed and therefore placing regulatory restrictions on such products will reduce choice and harm customers who can no longer obtain the deals they require to meet their needs or worse only have deals available to them on terms that are significantly worse.

Whilst we agree that healthy competition in the market place can encourage better deals for consumers, enhanced customer experience and improved customer satisfaction, there are certain areas which we do not think have been fully considered in this consultation. We do not consider that Ofcom has proved that longer contracts reduce competition. We are also concerned that Ofcom has failed to provide any evidence or analysis relating to the impact of linked contracts on customer behaviour or the stated harm to customers. We set out below our concerns in more detail.

IMPLEMENTATION TIMEFRAME

It is difficult to see why the changes must be implemented so early in 2020 when the implementation date of the EECC is not until December 2020. Ofcom maintains that it is a simple case of making changes to the terms and conditions yet has seemingly failed to take into consideration the full impact such changes will have on providers. Implementing change is a complicated process and one which involves significantly more than a change in terms and conditions. We will have to amend business plans and strategy in order to satisfy Ofcom's requirements to deliver the changes at a time when we have already made significant amendments at Ofcom's request, either as a result of legislation and General Conditions changes, such as Text to Switch, CLI, End of Contract Notifications, Annual Best Tariff; or, at the request of the regulator that the providers proactively agree to make changes such as Bundled Contracts. It is our view that providers who already adopt split contracts, will need significantly longer than three months. The implementation date proposed is not reasonable. If required to do so, we do not think we could adopt the changes without significant risk to the business before the end of Q4 2020 for the reasons set out above including dependencies on third parties providing customer services, billing and financing.

The impact of these measures will only impact a handful of providers. These affected providers are unfairly impacted compared with those providers who do not offer split contracts. The repercussions may lead to providers being unable to offer such competitive terms to consumers with a detrimental effect on competition.

IMPACT ASSESSMENT

Paragraphs 2.13 to 2.36 of Ofcom's consultation sets out its functions and duties to the consumer. Paragraph 2.37 confirms the requirement to properly impact assess regulatory proposals. In our view, the impact of the proposals set out in this consultation have not been conclusively laid out in this document in relation to split contracts.

Whilst there has been much focus on bundled contracts and switching and Ofcom's perceived impact on consumers regarding barriers to switching, there has been no consideration of what the impact to consumers would be if Ofcom removed the availability of 30 and 36 month contracts in their current form.

Ofcom states in 3.67 that "*Constraining customers' abilities to switch is likely to harm each of them individually*" yet does not specify how this harm will come about, nor the extent of the harm. Further, it is stated that the "*extent of the harm is likely to grow*" but again there is no evidential basis for making these statements – we would expect to see evidence of consumer complaints related to their inability to switch providers without paying off the handset.

Paragraph 5.16 states that it is Ofcom's view that it is "*self-evident"* that the requirement to pay a substantial sum is *"likely"* to deter switching. The impact assessment does not appear to be based on any research into, or evidential information from discussions with consumers. The consumer research mentioned in the consultation refers to bundled contracts, rather than split contracts. As outlined earlier, the evidence of a second hand phone market and provider run recycling schemes reveal that customers are selling their phones to realise capital, either to pay off their loans, or to invest in their next handset.

Ofcom considers that it has satisfied the tests set out in section 47(2) of the Communications Act 2003 because it has identified that "*consumers and other customers are harmed by the terms … in linked split contracts*." However, as previously stated, we do not think that Ofcom has proved the harm that they refer to, and moreover, their response repeatedly refers to 'likely' harm rather than of anything determined or proven. In acknowledging whether the test is satisfied, Ofcom's response is that it does not 'think' the measures would be unduly discriminatory. The lack of evidentiary data does little to determine whether Ofcom has satisfied the tests. One of the most important aspects of this test is 47(2) (b) which ensures the conditions imposed by Ofcom are not "such as to discriminate unduly against particular persons…". However, by reducing the term of a handset credit agreement, there will be a certain section of consumers who are unfairly disadvantaged. Those who are unable to afford devices over a 24 month period because the repayment costs over that timeframe are too expensive will certainly be adversely affected.

CONCLUSION

There has to be acknowledgement that consumers view their device, in the same way they view other expensive purchases. They acknowledge that they want the best they can afford and are prepared to enter into a credit agreement to do so. As with any purchases involving large monetary values, customers have the option to use credit to afford it.

As you will know, Tesco Mobile is regulated by the FCA and as such has a number of obligations when it comes to consumer credit lending. We are obliged to treat the customer fairly, make it clear that they are entering into a credit agreement, show the customer the monthly payments, explain what happens if they fail to make the payments, explain clearly that if they decide to move usage contracts they have to pay off the loan in full. The customer is fully aware of the time frames they are signing up to and are happy to do so. There is no evidence from the FCA's perspective of customer harm due to the length of credit agreements. We are not setting the prices for the devices, we are simply making them affordable for customers so that they have the widest choice available.

For the reasons set out in this response, we do not consider that Ofcom has adequately outlined sufficient evidence that linked contracts (of any length) causes harm to customers. We are providing a product that customers ask for. The demand in the market for such contracts indicates that the benefits offered outweigh Ofcom's concerns about the need to pay off the handset in order to switch airtime provider. Competition remains high with EE and Three expected to launch split tariffs as documented in the consultation.

We are happy to discuss this further.

Tesco Mobile Limited