Fairness in the telecoms market - The "loyalty penalty" and "switching"

Unsurprisingly, the **fair telecoms campaign** campaigns for fairness in the telecoms market.

This means accepting the reality of how markets will operate.

It also means that consumers should not be treated as professional buyers.

Economic theory suggests that effective competition will exert a lowering effect on prices, without the need for consumers to continually switch between providers of the same services.

If consumers need to be exhorted to continually switch, then this is an indication of market failure.

The effort involved in continually shopping around, simply to secure a fair price, has a direct implicit cost. The marketing activity, including third party organisations, involved in supporting switching imposes costs on the industry, which are ultimately reflected in higher prices.

What is referred to as the "loyalty penalty", most notably by **Citizens Advice**, is generally the effect of discounts being offered to switchers.

These discounts are nothing more than a reaction to the promotion of serial switching. All those who promote this activity must accept the inevitable consequences of what they seek.

Suggesting that all customers should benefit from the discounts offered to new or switching customers is simply nonsense.

Paying for handsets over a period

The way in which a fixed term of payments to cover the cost of a handset is bundled into the charge for on-going services, with a minimum term, is a scandal in its own right. This relates to the issue of the "loyalty penalty", but it is actually a separate issue and the two should not be confused.

The vital distinction is that between a "fixed term" and a "minimum term". Paying off the cost of a handset over a fixed number of monthly payments must cease when the payments have been made. Furthermore, it is wholly unacceptable for these payments (through their bundling in with fess for on-going services) to be subject to an inflation-based annual price adjustment.

It is imperative that **Ofcom** acts to cease this scandal, which some operators have already ceased for themselves.

Fair pricing

Whilst providers will always wish to offer incentives to win new business, this must not be allowed to distort the market – which includes existing customers in respect of on-going services.

Prices for on-going services must be stated for what they are, covering all those who are to pay them in the coming period. This is obviously different to the situation which applies to normal "one-off" purchases, where differences in price will be expected to occur over time.

It may be that discounts (or "cashbacks") are to be offered for on-going services, as an incentive for new customers or on account of the purchase of multiple services. These must however be declared separately from clear and straightforward pricing for each service.

Action by Ofcom

We have responded immediately to **Ofcom** instigating a discussion on its “fairness for consumers” project – see What Ofcom needs to do to ensure “fairness” for consumers.

Despite noises around the May legacy (New powers to fine firms that exploit consumer loyalty), we note a firm commitment to the role of the independent regulators in the letter to the **CMA** from Greg Clark (see Tackling the loyalty penalty: letter from Greg Clark, BEIS).

The action that **Ofcom** takes needs to firm, but focussed and well-considered.

Action so far has been minimal and disappointing.

Regulation and persuasion must steer the industry away from the unfairness found in many areas.

This has to be backed up by the threat of necessary intervention, but compliance rather than punishment must be the objective.

In pursuing fairness, in practice and in effect, rather than by the wording of commitments, it is necessary for **Ofcom** to hold sufficient powers of intervention. In particularly bad cases, these could be supported by the further powers of the **CMA**.

It is however important that proper standards are set for and by the industry itself, driven by **Ofcom**. Specific regulation and, even more so, legislation tends to set minimum standards which become the norm.

A competitive market must be seen to be driving standards up (and forcing prices down). Excessive intervention can have the effect of enforcing only minimal standards.

Comments on the Citizens Advice approach

Demands from **Citizens Advice** appear to demonstrate a total lack of understanding of the market and the true needs of consumers. The Loyalty Penalty – which it opposes, is an inevitable consequence of serial switching – which it advocates and actively encourages.

Discounted introductory prices must be recognised for what they are – an inevitable feature of a market in which providers are competing for new and switching customers. It is absurd to suggest that all customers should benefit from such discounts, or be compelled to switch to do so.

Serial switching places unreasonable demands on citizens. It also introduces additional overhead costs to the industry, in marketing effort, which will ultimately be reflected in higher prices.

The notion of consumers being automatically switched is essentially a demand for the retail side of the industry to be nationalised, with provision being allocated by the government based on price.

The idea that all consumers must be given the benefit of all discounts that may be offered is total nonsense. Suggesting that this radical principle be applied only to one segment of the sector is bizarre and incoherent.

We urge **Citizens Advice** to gain a deeper understanding of telecoms and its markets. This is vital if it is to bid to take on the role of the Independent Consumer Advocate for this sector.