Competition & Markets Authority

Tackling the loyalty penalty

Response to a super-complaint made by Citizens Advice on 28 September 2018

19 December 2018

Website: www.gov.uk/cma

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Executive summary

1. In some markets, longstanding customers can pay much more than new customers for the same services – this is known as the ‘loyalty penalty’. This happens when suppliers charge higher prices to their existing customers, who they think are unlikely to switch to get a better deal. The result is that in many cases, people who stay with their supplier end up paying significantly more.

2. This is the basis of the super-complaint that Citizens Advice made to us. It highlighted concerns that not enough has been done to tackle loyalty penalty issues in five markets: mobile; broadband; cash savings; home insurance and mortgages.

3. Many services are paid for through automatically renewed or rolled over contracts. While this can be convenient for customers, it also increases the risk that customers who get rolled over year after year will pay a loyalty penalty. This super-complaint has given us the opportunity to look at this practice across markets, what has been tried in different markets over the years and consider what more can be done to prevent the loyalty penalty.

4. Overall, we have found that the loyalty penalty is significant and impacts many people, including those who can least afford it. Customers rightly feel ripped off, let down and frustrated. They should not have to be constantly ‘on guard’ or spend hours negotiating to get a good deal. This erodes people’s trust in markets and the system as a whole.

5. Not enough has been done in the past by the CMA and regulators; there needs to be a step-change to tackle these problems more effectively. The focus should not only be on giving better support to consumers; but getting tough on harmful business practices and using targeted pricing interventions where needed to protect those who suffer most, particularly those who are vulnerable.

6. Our response sets out a significant package of reforms, both across markets and in the five markets, to address this issue and ensure that consumers can get better and fairer outcomes. The FCA and Ofcom are actively looking at this issue in the five markets. We welcome that work and make a number of recommendations in those markets.

How big is the problem?

7. There is a substantial loyalty penalty paid by consumers each year. Existing estimates suggest this penalty could be around £4 billion in total across the

five markets we have looked at. The number of people who pay a penalty varies by market, with estimates ranging from under one million in mortgages to over 12 million in home insurance. This does not mean that prices are too high overall because some people are paying much lower prices, but some people are clearly paying too much.

8. These are the best estimates based on available data, but there are still gaps in the evidence base. Collecting and publishing information regularly on the size of the loyalty penalty and who pays it in key markets is important. This will improve understanding by regulators, raise public awareness and hold businesses accountable.

9. The loyalty penalty is not just a problem confined to the five markets. It is likely to be a much wider issue potentially arising in many other markets, for example in pay TV, roadside assistance, many other insurance markets, pensions and other subscription services such as online gaming, software and magazines.

Why does the loyalty penalty arise?

10. Many services are paid for through contracts which automatically renew or roll over, often on a higher rate. The result is that customers pay more for the same service unless they actively intervene:

    - in some markets there is a sharp increase after the introductory price ('price jump') like in energy;
    - in others there are successive price rises ('price walking') as in insurance; and
    - elsewhere customers on older tariffs sometimes pay higher prices for similar services ('legacy pricing'), as in broadband.

11. In all cases longstanding customers can end up paying much more than new customers. There are many different reasons why customers remain with their supplier. They are not necessarily being actively 'loyal' to a particular brand or supplier. Some people wrongly believe that staying will pay off in the long term, do not know they could make significant savings or have other things to worry about, so do not even think about switching. It can also be confusing and time consuming to shop around, and suppliers can exacerbate these problems. In some cases, the saving is small and is not enough to be worth worrying about.

When is it most problematic?

12. Offering introductory deals is not necessarily harmful. It can encourage people to shop around and try out new services, as well as allowing new businesses a foot in the door by attracting new customers. The loyalty penalty raises particular concerns when:

    - suppliers make it more difficult than it needs to be for customers to exercise choice, and then exploit those who do not switch;
    - the price gap is large, with some paying very high prices, or it affects many people;
    - it particularly harms those who may be vulnerable such as the elderly, those on low incomes, or with physical disabilities or poor mental health;
    - it happens in 'essential' markets.

Who is hit hardest by the loyalty penalty?

13. The loyalty penalty affects many consumers across different markets and at different points in time. The exploitative practices used by some suppliers can cause serious problems for all consumers, who do not have the time or are not able to take the steps necessary to avoid paying a penalty.

14. The most vulnerable in our society can have even greater challenges engaging in markets, such as those on low incomes, people who struggle to use online services, or people with poor mental health who may avoid or fear change. This means they may be more at risk of paying the loyalty penalty and may be least able to afford it. It is therefore important that the needs and capabilities of vulnerable consumers be taken into account when looking at tackling the loyalty penalty.

15. Protecting the interests of vulnerable consumers is a priority area for the CMA. We have an ongoing programme of work underway to better understand the challenges vulnerable consumers can face in markets, and how we can help to address them.

What role do businesses play in this?

16. Suppliers can also be a big part of the problem, as well as being a key part of the solution to enable customers to get better deals. Businesses across a wide range of markets can make it much more difficult for existing customers to engage and penalise them if they are not constantly checking the deals they are getting. We have identified a range of practices, which we consider to be unacceptable. These include:

- making it more difficult to leave a contract than it is to sign up;
- rolling over customers onto new contracts without sufficient warning;
- imposing 'stealth' increases in price on renewal year after year, which can lead to very significant price increases without customers being aware of it; and
- requiring customers to auto-renew or get rolled over when they take up a service or buy a product; in most markets there should be a choice.

17. We recognise that auto-renewal can benefit consumers, particularly when there are harmful consequences from not renewing. However, suppliers must stop taking advantage of their existing customers by charging much higher prices, misleading people about their offers and making it much more difficult for customers to get good deals than it needs to be. These practices are likely to impose a significant cost on the economy, both in terms of the time consumers spend trying to get better deals and because they can end up paying much more. This makes people feel that markets are working against their interests and undermines trust.

18. Action has been taken by regulators and the CMA to try to tackle these problems. However, the prevalence of these issues across many markets shows that there is much more for us to do to stop these types of practices by businesses.

19. We are taking enforcement action in the anti-virus software market, and this is a first step in a wider programme of enforcement. We will also be considering whether existing law should be changed to ensure these practices are stopped.

What more should be done to tackle the loyalty penalty?

20. The CMA, regulators and government must together tackle these problems head on. While there have been efforts to do so, these have not had sufficient impact. In the past too much has been asked and expected from consumers, and not enough from businesses. Although we have become better at designing more effective interventions, more can be done, particularly to protect vulnerable consumers.

21. Suppliers should do all they reasonably can to support their customers in getting the best deal, rather than exploiting any perceived weaknesses or biases. We encourage businesses to work together with regulators to achieve this, rather than frustrating or delaying attempts to fix these issues.

22. There is also a strong case for considering more direct intervention such as price controls, targeted to protect those who are worse off. These have been

used before by the CMA and regulators in some cases, particularly to protect vulnerable consumers. And they should be considered in other markets. We make a number of recommendations where such interventions should be considered by regulators, alongside other measures, in the five markets highlighted by Citizens Advice.

23. It is also important that customers are given greater support and the tools they need to make active and informed choices. This ensures that businesses are put under continued and greater competitive pressure. There are newer and bolder ways to do this which could transform some markets and make it much easier for consumers to get better deals.

24. Based on our review we consider that the best ways to achieve change are:

- providing genuine support to consumers through the use of 'smart data' (data-driven technologies and services to help consumers), using intermediaries (including price comparison websites, automatic switching services, or local face-to-face advisory services) and 'collective switching' which offers exclusive tailored deals;
- enforcement against businesses to tackle harmful and unacceptable practices; and
- considering targeted direct pricing interventions either to limit price differences, such as restricting price walking, or price caps, where there is clear harm, in particular to vulnerable consumers.

Our package of reforms across markets

25. We are recommending eight key reforms to address the problems related to the loyalty penalty.

A. Stopping harmful business practices

26. The CMA and regulators should continue to take action against suppliers whose business models are harmful to consumers. This means using our existing consumer enforcement powers and the powers regulators have to intervene directly, and strengthening these powers where needed.

    1. Bolder use of existing enforcement and regulatory powers to tackle harmful business practices. We are launching investigations in the anti-virus software market. [Recommendation to regulators and action by the CMA].

    2. Legislative and/or regulatory change may also be needed to effectively tackle these practices and we will be exploring this further, alongside new powers for the CMA to seek substantial fines where law is breached. [Recommendation to government].

We have developed a set of core principles for businesses to follow across markets and we will be building on these, alongside considering whether these should be explicitly covered in existing law. These include:

i. exit/entry equivalence: people must be able to exit a contract at least as easily as they can enter it;
ii. auto-renewal should generally be on an 'opt in' basis upfront, and include a clear and prominent option without auto-renewal in most markets;
iii. exit fees should not be used after any initial minimum/fixed term;
iv. auto-renewal onto a fresh fixed term should not generally be used;
v. customers must be sufficiently informed about the renewal and any price changes (through sufficient notifications) in good time; and
vi. switching should generally be managed by the gaining supplier so that customers do not have to contact their existing supplier if they want to move.

B. Publicising the loyalty penalty to hold suppliers to account

27. Reputational measures designed to put pressure on businesses can have a real impact in markets. In this case, data on the scale and size of the loyalty penalty, and which suppliers have the highest price differences, can put pressure on them to reduce this gap.

3. Publish the size of the loyalty penalty in key markets and for each supplier, through for example an annual joint loyalty penalty report. [Recommendation to regulators].

C. Giving people more help in getting better deals

28. The CMA and regulators have relied too heavily on 'information remedies' to help consumers, which have had limited impact. In recent years we have got better at developing and testing more intelligent 'nudges', and these can make a difference for some customers. But they are not always sufficient, particularly for the hardest to reach consumers. Many people need even more support.

4. Empower intermediaries to support switching for example, giving a greater role to local consumer-facing advisory organisations, such as Citizens Advice, who could more actively support switching for vulnerable consumers. [Recommendation to government].

5. Press ahead with the Smart Data Review and rolling this out in those markets such as telecoms, where it has the greatest potential to transform markets. [Recommendation to government and regulators].

6. Capture and share best practice on 'nudge' remedies that have been tested and shown to work or not. Some remedies (such as requiring suppliers to give last year's price on renewal) could be rolled out across markets and potentially strengthened. [Recommendation to regulators and the UK Competition Network].

D. Protecting consumers from harm, particularly vulnerable consumers

29. Regulators have in the past been reticent to introduce price caps because these can distort markets. But where people who are unable or find it very difficult to switch are paying significantly higher prices, the case for targeted intervention is stronger.

7. Consider targeted pricing regulations such as limiting price differentials or price caps, alongside other measures where there is clear harm, particularly to protect vulnerable consumers. We also make recommendations about potential pricing interventions to be considered as part of ongoing work in the five markets. [Recommendation to regulators and the CMA].

E. Better understanding of the loyalty penalty across markets

30. It is also important to have more robust data on the extent of the loyalty penalty across a number of key markets, and who is paying it. This is currently assessed on an ad hoc basis through specific market studies. But this approach does not enable comparisons across markets, nor, crucially, does it allow regulators to identify whether the same individuals are worse off across markets and over time.

8. Assess the feasibility of matching price data to a recurring, large scale UK survey to improve our understanding of who pays the loyalty penalty across markets, and whether vulnerable consumers are particularly adversely affected. [Recommendation to regulators].

Our recommendations in the five markets

31. Alongside these cross-cutting recommendations, we have also looked at each of the five markets highlighted by Citizens Advice. We have considered what actions have previously been taken, what can be learnt from our review and

what more can be done to tackle the loyalty penalty in these markets. We have worked with the regulators to understand these markets.

32. Based on our review, we also make recommendations to the FCA and Ofcom on measures to tackle the loyalty penalty in the five markets, which should be considered as part of their current work in these markets, alongside any other potential remedies.

Mobile

33. We do not consider that providers should continue to charge customers the same rate once they have effectively paid off their handsets at the end of the minimum contract period. This is unfair and must be stopped. We welcome Ofcom's recent consultation on this.

- We support a requirement on mobile providers to move customers on bundled handset and airtime contracts onto a fairer tariff when their minimum contract period ends. [Recommendation: Ofcom].
- In addition, Ofcom should seek to increase the engagement and awareness of consumers by pushing forward with implementing smart data, supporting the development of innovative intermediaries, and tackling low levels of awareness of SIM-only deals. [Recommendation: Ofcom].

Broadband

34. Loyalty penalty problems in this market must be thoroughly investigated and we welcome the review recently launched by Ofcom. As part of its review we recommend that:

- Ofcom consider a number of possible pricing interventions including tackling broadband legacy pricing and targeted safeguard caps to protect vulnerable consumers, alongside measures to increase engagement such as the use of smart data and exploring the feasibility of collective switching. [Recommendation: Ofcom].

Cash savings

35. The FCA has recognised that interventions to date have had limited impact on addressing the harm to longstanding customers, and it is currently considering a 'Basic Savings Rate' among other potential interventions. We welcome this further work and recommend that:

- If the FCA implement the Basic Savings Rate, it evaluates whether this has had the intended impact and if not, consider further pricing interventions such as a targeted absolute price floor in cash savings. The FCA should also consider whether collective switching can be applied. [Recommendation: the FCA].

Insurance

36. Evidence suggests that many longstanding customers are paying much more than newer customers, with businesses repeatedly increasing prices year on year. Therefore, we welcome the FCA's current market study and as part of this study we recommend that it:

- Investigate insurance pricing practices and consider pricing interventions that limit price walking, for example rules to restrict this practice. [Recommendation: the FCA].

- Explore how intermediaries can continue to benefit the home insurance market (for example where 'semi-smart' solutions can improve the existing infrastructure of price comparison websites). [Recommendation: the FCA].

Mortgages

37. In mortgages, the FCA is currently undertaking a market study. It is taking immediate action to tackle those who cannot switch in this market (ie 'mortgage prisoners') by helping these customers move onto better tariffs, where feasible. We strongly support that work, but there are still 10% of longstanding customers who could switch and make significant savings but do not. We recommend that:

- The FCA find out more about mortgage customers who could switch but do not and look at what measures can be taken to help or protect them if needed. [Recommendation: the FCA].

What next?

38. We believe a step-change in approach is needed to effectively tackle these issues. We have set out a package of reforms, both across markets and specifically in relation to the five markets identified by Citizens Advice. We believe these will achieve real changes and help existing customers get a fair deal.

39. A number of the market-specific recommendations can now be taken forward by regulators through their existing studies or ongoing work in each of these

markets. Some of the recommendations require further consideration and oversight by the CMA and others such as government and regulators.

40. The CMA will be undertaking further work on the loyalty penalty, working closely alongside regulators, government, business and organisations such as Citizens Advice. This project will take forward in particular:

- recommendation 1, where we are launching enforcement cases;
- recommendation 2, a review of the case for changing consumer law in addressing the loyalty penalty; and
- recommendation 8, exploring the feasibility of matching price and survey data.

41. We will provide an update on our progress to the newly established joint government-regulator Consumer Forum, led by the Minister for Consumer Affairs, in six months. An update will also be published on our website. The FCA and Ofcom will also provide an update on their progress in the five markets.

42. The Consumer Forum provides an important opportunity for us to work more closely together. We support its development and continued oversight on key consumer issues such as tackling the loyalty penalty across key markets and addressing the challenges faced by vulnerable consumers.

43. We have considered Citizens Advice's request that we undertake a market study into the loyalty penalty across the five markets. We do not believe this is the right approach at present, given the work we have already done and the project we will be undertaking to take forward our cross-cutting recommendations. In relation to the five markets, our recommendations to regulators can be taken forward now in their ongoing work without the need for a market study. We consider this is the most efficient way to achieve results quickly.

44. We will look at whether sufficient progress has been made in taking forward our recommendations over the next 12 months. At that stage we will reconsider what next steps are necessary, such as whether a market study is needed. The CMA is committed to continuing to drive this work forward to maintain momentum and ensure changes are achieved.

1. Introduction

1.1 This chapter provides an overview of the super-complaint process, the issues raised by Citizens Advice and our approach to this investigation.

The super-complaint process

1.2 This document is the reasoned response of the Competition and Markets Authority (CMA) to the super-complaint entitled 'Excessive prices for disengaged consumers', submitted by Citizens Advice to the CMA on 28 September 2018.[1]

1.3 A super-complaint is a complaint submitted by a 'designated consumer body' that 'any feature, or combination of features, of a market in the UK for goods or services is or appears to be significantly harming the interests of consumers'.[2] Citizens Advice is a designated consumer body.[3]

1.4 The CMA is required to consider the concerns raised and publish a response within 90 calendar days setting out whether or not it has decided to take any action and, if so, what action it proposes to take. The response must state the reasons for the CMA's proposals.[4]

Issues raised in the super-complaint

1.5 In its super-complaint, Citizens Advice raised concerns that people who stay with their provider in 'essential' service markets, often on default or roll over contracts, end up paying significantly more than new customers for the same goods or services. It referred to this as a 'loyalty penalty'. It was concerned that this lead to significant harm to consumers, in particular vulnerable consumers such as those on low incomes, with mental health problems, low levels of education and the elderly.

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[1] Citizens Advice, *Excessive prices for disengaged consumers: a super-complaint to the Competition and Markets Authority*, September 2018.
[2] Enterprise Act 2002 (EA02), section 11(1).
[3] The Secretary of State for the Department of Business, Energy and Industrial Strategy (BEIS) can make any organisation a designated consumer body, provided they represent the interests of consumers of any description and also meet any other criteria published by the Secretary of State which are applied when determining whether to make or revoke a designation. It is expected that those designated will be informed bodies who are in a strong position to represent the interests of groups of consumers and able to provide solid analysis and evidence in support of any super-complaint they may make.
[4] EA02, section 11(2) and 11(3).

1.6 The super-complaint focussed on five 'essential' markets:[5] mobile and broadband, regulated by the Office of communications (Ofcom); cash savings, home insurance and mortgages, regulated by the Financial Conduct Authority (FCA). Across these five markets, Citizens Advice estimated that individual consumers can pay a loyalty penalty of almost £900 per year.

1.7 It identified the following concerns:

- the loyalty penalty is widespread, as a large number of people are on uncompetitive deals, paying more for a service than a new customer would;
- consumers do not realise that they are being penalised for staying with their supplier and face obstacles when trying to switch or shop around to get a better deal;
- consumer inertia is being exploited through long lasting automatically renewing contracts that allow price increases at renewal; and
- consumers in vulnerable situations are disproportionately impacted by the loyalty penalty.

1.8 The super-complaint asked the CMA to undertake a cross-sectoral investigation into these issues and propose recommendations and remedies that can be implemented by the CMA, regulators and government. It expected the CMA to consider:

- what more can be done to encourage consumers to engage in markets where the loyalty penalty exists;
- what direct interventions into these markets are necessary to protect consumers from exploitation; and
- what specific protections for vulnerable consumers who pay the loyalty penalty are necessary.

Evidence we assessed

1.9 To inform our response, we examined a range of evidence. This includes work and analysis undertaken by Citizens Advice, including various reports published on the loyalty penalty in the five markets,[6] and their complaints

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[5] These markets were those in which Citizens Advice was able to identify or gather relevant evidence. However it noted that there are likely to be additional markets where there are similar concerns. The super-complaint did not explicitly include energy as one of these markets, although it referred to this market in the evidence it presented.
[6] The reports are: Citizens Advice, *Exploring the loyalty penalty in the broadband market*, April 2017; Citizens Advice, *Exploring the loyalty penalty in the mortgage market*, July 2017; Citizens Advice*, The insurance loyalty penalty: unfair pricing in the home insurance market*, November 2017; Citizens Advice, *The cost of loyalty: exploring how long-standing customers pay more for essential services*, February 2018; *Citizens Advice, Hung up on the handset: an investigation into sales practices in the mobile phone market*, April 2016.

database. Citizens Advice also provided further views on remedies and their application to the five markets.

1.10 In addition, we issued a general invitation to comment and received 41 submissions from a range of stakeholders, including academics, businesses, charities, consumer bodies and industry bodies, as well as 31 submissions from individual members of the public. Annex A lists those organisations from which we received submissions. We also assessed datasets submitted to us by Ismybillfair and Money Advice Service, engaged with academics, and reviewed the existing evidence base through desk research.

1.11 We also worked with Ofcom and the FCA to inform our understanding of the issues, any previous and ongoing work and measures put in place in the five markets (see Annexes C and D for more detail). We have also liaised with government to understand other relevant developments, including relevant follow up work being undertaken as a result of its consumer green paper published earlier this year.[7]

1.12 Alongside this, we collected evidence from consumers' reports of their own experiences in the five markets and elsewhere. For example, we used online forums, desk research, the complaints databases held by Ofcom and Citizens Advice, evidence provided by the ombudsman in financial services and telecoms, and work undertaken previously by the CMA.

1.13 We consider vulnerable consumers throughout our response, drawing on our existing programme of work which we launched earlier in 2018 as a priority area.[8] This work has focussed on understanding the different dimensions of consumer vulnerability across markets, and considered how the CMA can help. As part of this, we commissioned qualitative research with vulnerable consumers to better understand their experiences of key markets including mobile, broadband and insurance.[9] A separate paper setting out this broader work on vulnerable consumers will be published in the new year.

1.14 We would like to thank all those who have assisted us in our investigation.

[7] Department for Business, Energy and Industrial Strategy, *Modernising consumer markets consumer green paper*, April 2018.
[8] The 2018/19 Annual Plan identified vulnerable consumers as a priority focus for the CMA. This has continued in the draft 2019/20 Annual Plan (under consultation at the time of writing).
[9] Full details of the commissioned research and its findings are available on the CMA's vulnerable consumers webpage.

Structure of this response

1.15 The remainder of this response is structured as follows:

- Chapters 2 outlines what the loyalty penalty is, why it arises, when it is most problematic;
- Chapter 3 defines consumer vulnerability and considers the additional challenges to switching and negotiating which vulnerable consumers can face;
- Chapter 4 estimates the size of the loyalty penalty in the five markets and who pays it;
- Chapters 5 to 8 set out: different approaches to tackling the loyalty penalty, including helping consumers to engage and switch; principles to stop harmful business practices; and regulating prices. These chapters consider the different types of remedies, what has been tried previously by regulators, and how these types of remedies might be applied in each of the five markets; and
- Chapter 9 presents the CMA's conclusions and recommendations and sets out next steps for further work.

1.16 Throughout this response, where we refer to regulators, this also includes the CMA which can investigate and put in place remedies where it finds problems in unregulated markets.[10]

[10] For example, we can undertake market studies or market investigations in both regulated and unregulated markets.

2. What is the 'loyalty penalty' and when is it most problematic?

- The loyalty penalty arises because some people are less likely to switch or negotiate, and businesses choose to charge them more while offering new customers lower prices. This means some people can pay much higher prices, whereas others pay lower prices.
- This practice occurs in a number of auto-renewal and subscription markets, in addition to the five markets highlighted by Citizens Advice.
- Allowing suppliers to charge different prices to different customers has benefits: introductory offers encourage consumers to try out new products they would otherwise not have purchased and some consumers receive lower prices.
- The loyalty penalty is of greatest concern when:
  - it involves confusing or misleading customers, leading to poor decision making or undermines trust in markets;
  - market characteristics suggest it is likely to increase average prices for consumers;
  - it leads to harmful distributional effects;
  - the product or service is considered 'essential' or constitutes a large proportion of people's expenditure.
- It is particularly concerning when those that suffer are vulnerable, where they are unable to act to avoid the penalty, or they are not aware of it.

Introduction

2.1 This chapter explains what we understand by the term 'loyalty penalty', the causes underlying it, and the factors that regulators should take into account when considering an intervention to tackle it.

2.2 The chapter is structured as follows:

(a) what is the loyalty penalty?

(b) why does the loyalty penalty arise?

(c) what markets does the loyalty penalty arise in?

(d) when is the loyalty penalty most concerning? and

(e) conclusion.

2.3 We have also assessed available evidence on the five markets highlighted by Citizens Advice - mobile, broadband, cash savings, home insurance and mortgages - in relation to the criteria we set out for determining when the loyalty penalty is most concerning. We apply these criteria to the five markets in Annex B. In some cases, further work is required to develop this evidence, which will be a key part of the ongoing work by Ofcom and FCA in these markets (detail on these markets and the work undertaken is set out in Annexes C and D).

What is the loyalty penalty?

2.4 Throughout our response we apply the term used by Citizens Advice – 'the loyalty penalty' – to refer to the situation where, on average, businesses charge higher prices to existing customers who stay with them, than they do to new customers or those who negotiate.[11] This can result in longstanding customers paying significantly more than other customers.

2.5 The loyalty penalty is a form of price discrimination, where customers are charged different prices for the same product or service despite having the same costs to serve.[12] This leads to some people paying more than others. Price discrimination can arise where customers differ in their willingness or ability to pay for the good or service (for example, students are offered discounted cinema tickets).

2.6 As explained in more detail in this chapter, price discrimination can have some benefits. Some consumers receive low prices and it can also encourage more people to switch, driving competition that can benefit us all.

2.7 In the case of the loyalty penalty, the price discrimination is based on variation in customers' tendency to stay with their existing provider without negotiating. It arises from the following types of pricing practice:[13]

- situations where at the end of a contract customers who do not switch or negotiate are automatically subject to a one-off price jump onto a higher rate ('price jump');

[11] Or in the case of savings, worse interest rates.
[12] More precisely price discrimination is where different mark ups over cost are charged to different customers. This contrasts with 'uniform pricing' where all customers pay the same price, and 'cost-based pricing' where some customers pay more than others because they cost more to serve.
[13] Together we refer to these as 'loyalty penalty pricing'.

- gradual price increases over time that vary across customers depending on tenure, and may also depend on the customer's previous response to price increases, or on other customer characteristics ('price walking'); or
- the introduction of new, cheaper tariffs or better products while retaining expensive legacy deals for existing customers ('legacy pricing').[14]

2.8 An example of a price jump occurs in broadband or energy, where customers are often moved onto a higher price after the expiry of their initial contract term. Price walking happens in some insurance markets where customers can face price rises each time that their contract is renewed or auto-renewed. Legacy pricing arises in some cases in mobile and broadband. For example, some people could upgrade their broadband at no extra cost as the gap has narrowed between the prices of superfast and standard broadband.

2.9 It is not the case that all longstanding customers pay higher prices. Some customers have assessed their options and negotiated a lower price with their supplier, and so are not paying a loyalty penalty. Some may stay because they prefer the product or service offered by their existing provider.

2.10 However, longstanding customers often include those who have been unable, or struggled to switch or negotiate. This may be for a variety of reasons which we explore in this chapter. Understanding the causes and effects of the loyalty penalty, including which consumers gain from the penalty and which lose out, is important for determining where regulators should intervene to tackle it.

Why does the loyalty penalty arise?

2.11 The underlying causes of the loyalty penalty are:

- customers differ in terms of their likelihood and ability to negotiate or switch provider in response to a price rise;[15] and
- businesses are able to charge higher prices to customers who are less likely to negotiate or switch, and they choose to do so.

2.12 This section explains these two causes in more detail. In Annex B we identify some of the reasons why consumers do not switch or negotiate in the five

[14] We are not including within this situations where customers on fixed price deals may be charged different rates depending on varying market conditions at the point in time when they entered into the fixed price deal (for example, the interest rates on two-year fixed rate mortgages entered into at the start of the year may differ from those for two-year fixed rate mortgages entered into at the end of the year if expectations about future interest rates changed over the course of the year).

[15] In this context, it is possible that a customer who places a very high value on the product to nevertheless be very price sensitive, because they shop around and switch provider regularly, and as a result receive a low price. On the other hand, a customer with a lower valuation that is 'loyal' to their provider can end up paying the higher price.

markets that were highlighted by Citizens Advice, and we describe the types of loyalty penalty pricing that occurs in these markets.

Why some people are less likely to switch or negotiate

2.13 Shopping around for a good deal is generally not a costless process. In some cases, it can be relatively straightforward (for example, comparing prices of a book and making a purchase online). In other cases, it can be a time consuming or difficult process for customers to:

(a) access information about the various offers available to them at the right time;

(b) assess these offers; and

(c) act on this information and analysis by purchasing the good or service that offers the best value to the customer and meets their requirements.[16]

2.14 In thinking about the factors that can affect how likely customers are to switch or negotiate in response to a high price, it is helpful to distinguish between:[17]

(a) features of the market that make it more difficult for all customers to shop around or move to get better deals;

(b) behaviours and characteristics of consumers that make it more difficult for them to access, assess and act on information about the costs and benefits of the different options available to them; and

(c) behaviour by businesses that makes search and switching more difficult or makes it more difficult for customers to make effective decisions.

2.15 Market features could include complex products which create search costs by making it difficult for customers to access and assess information,[18] or the possibility of interrupted service which may raise the cost of switching. In the extreme, some customers may be unable to switch (for example where there is only one provider). Although search and switching costs are present for all customers, their impact and likelihood may be greater for some customers

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[16] For more discussion of this framework, see OFT, *What does behavioural economics mean for competition policy?*, 2010

[17] For more discussion, see UKCN, *Helping people get a better deal: learning lessons about consumer facing remedies*, October 2018.

[18] For example, in the case of mobile it can be difficult to compare network quality (which may vary in terms of reliability, speed and coverage) and customers may need to understand their expected patterns of usage (eg how many minutes and how much data they require) in order to choose the most appropriate tariff.

than others, as explained in more detail in the next chapter on vulnerable consumers.

2.16 Consumers' behaviours and characteristics, including the context in which they make decisions, can also make them less able or likely to access, assess and act on information that could lead to switching or negotiating. These can be permanent, temporary or situational factors that mean customers vary in how high the costs of switching or negotiating are (or their perceptions of these costs), and how able they are to overcome them. For example:[19]

- When accessing and assessing information about alternative deals, customers can be overwhelmed by 'choice overload',[20] or make poor decisions because they are influenced by irrelevant information[21] or how the choices are presented.[22] Some customers have less time or do not have access to digital tools that make searching easier. Some may have misconceptions, for example, thinking it is more time consuming or difficult to search than it really is or being unaware that they can get a better price by switching or negotiating.

- When considering whether to act, people tend to stick with the default or their previous decision,[23] or delay taking.[24] As avoiding the loyalty penalty often requires action at a specific time (for example, where an annual contract is due for renewal), people can lose out through inattention. Some people may also perceive switching to be more risky or difficult than it really is. They may vary in their appetite to take on that risk, find it more difficult to switch (for example because of differing abilities or financial skills or because they are preoccupied with other aspects of their life - see chapter 3), or they may feel a relational bond with their current provider.

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[19] For more detailed discussions of behavioural biases see *OFT, Consumer behavioural biases in competition – a survey*, 2011, OFT, *Consumer contracts*, 2011, *FCA, Applying behavioural economics at the FCA: occasional paper no. 1*, 2013.

[20] Iyengar, S. and Lepper, M. *When choice is demotivating: can one desire too much of a good thing?,* Journal of Personality and Social Psychology, 2000.

[21] This is known as 'anchoring' - where decisions are made along a numerical spectrum (eg deciding how much insurance to take out), information that may seem trivial or irrelevant can anchor consumers and substantially shift their behaviour. See Tversky, A. and Kahneman, D. *Judgment under uncertainty: heuristics and biases,* Science, 185(4157), pp 1124-1131, 1974.

[22] This is known as 'framing' - the phenomenon where individual's preferences shift when the same choice is presented, or 'framed', in different ways. See Tversky, A. and Kahneman, D. *The framing of decisions and the psychology of choice*, Science, 211(4481), pp. 453-458, 1981.

[23] This is known as 'status quo bias'. See Samuelson, W. and Zeckhauser, R. *Status quo bias in decision making*, Journal of Risk and Uncertainty, 1(1), pp7-59, 1988.

[24] This can be caused by 'present bias' where individuals tend to place disproportionate emphasis on the present; focus on the more salient benefits of present consumption and tend to discount the future costs involved. See Barber, B.M., Odean, T. and Zheng, L. *Out of sight, out of mind: the effects of expenses on mutual fund flows*, Journal of Business, 78(6), pp.2095- 2119, 2005.; Shui, H. and Ausubel, L. *Time inconsistency in the credit card market*, 2004.

2.17 The behaviour of suppliers can amplify the costs of switching[25] or exploit the difficulties people having in making decisions. In particular, auto-renewal or roll over contracts,[26] though often helpful, can make people less likely to switch. Businesses may also provide insufficient warnings prior to customers being auto-renewed or fail to make it clear that a price rise has occurred.

2.18 In some markets there may be disproportionate exit fees or businesses may place other obstacles in the way of searching or switching, such as requiring customers who wish to switch to call during limited business hours. The range of such harmful practices is discussed in more detail in chapter 7. The effect of these can vary across people depending on their characteristics, such as the amount of time or 'mental bandwidth' they have to spend on the issue.

2.19 Some of these issues emerged from our commissioned qualitative research, which explored people's views and experiences of switching.[27]

> 'It's sometimes very difficult to compare deals because it's not comparing like with like because some insurance policies include things but others don't.'
>
> 'You know, it's so easy for me to swap car insurance or home insurance but when it's something like gas and electric, I'm just scared that it will stop, and I'll be left with nothing for a few days.'
>
> 'I've also been with [telecoms provider] for ages and ages. They are quite good, but I would move. It's just the hassle. I can't be bothered to spend hours and hours on the phone to them. So, I'd rather just stay with them. I don't think I'm getting a particularly good deal.'

Why suppliers are able to charge higher prices to customers who are less likely to negotiate or switch

2.20 In order to be able to price discriminate, businesses must either be able to identify and separate different groups of customers, or be able to set their prices in a way that reveals their likelihood of switching or negotiating.[28] In the

[25] For a detailed review of switching costs, see OFT, *Switching costs*, 2003.
[26] An automatic renewal or continuation of a contract after the expiry of the current term, unless one of the involved parties gives a notice of its discontinuation
[27] See chapter 3 for more details. The full research findings are available in the published report by BritainThinks, available on the CMA's vulnerable consumers webpage.
[28] Businesses must also be able to prevent customers who buy at a low price from being able to sell the product or service on to other customers at the high price. This is unlikely to be an obstacle where customers have accounts that are linked to their identity.

case of the loyalty penalty, businesses can do this by observing the customer's tenure and whether they have negotiated, or other characteristics that indicate their willingness to switch. Businesses do this because it is more profitable. It allows them, for example, to reduce their price to customers who are more likely to switch, without having to also offer price cuts to other, less price sensitive, customers (losing further profit).

2.21 The extent of such price discrimination could increase further in future if businesses have greater access to data on their customers, and improved tools for using it. This would enable the tailoring of price rises to become more precise. For example, suppliers could use this data to vary annual price increases across customers, based on characteristics that indicate to them that the customer is particularly unlikely to switch away in response to a high price.[29] Such 'personalised pricing' is the subject of a current CMA and BEIS research project.[30]

What markets does the loyalty penalty arise in?

2.22 The loyalty penalty can arise in markets where consumers make regular purchases (in contrast with markets where people make infrequent or one-off purchases). In these markets, customers sign up to make regular payments, and the end of each lower priced fixed term contract is followed by an automatic renewal for a new fixed term or the customer is moved onto a rolling or default contract (unless the customer actively intervenes).

2.23 This occurs in a range of markets including: utilities, such as energy; telecoms such as broadband and mobile; and financial services, such as cash savings, insurance and mortgages. It can also occur in other markets with 'subscription' services. Loyalty penalty pricing may therefore become more common as subscription services become more prevalent.[31]

2.24 Aside from the markets identified by Citizens Advice, it might also arise in other auto-renewal, roll over or subscription products or services such as:

- other insurance markets (eg car or health insurance or breakdown cover);
- pay TV;
- film or music streaming;
- online gaming;

[29] For a more detailed discussion of personalised pricing, see *OFT, The economics of online personalised pricing*, 2013.
[30] CMA, *Government and CMA to research targeting of consumers through personalised pricing*, 2018. See also FCA, *Feedback statement on Big Data Call for Input*, 2016.
[31] See, for example Zuora, *A nation subscribed: 2017 state of the UK subscription economy,* 2018.

- software;
- credit checking services; and
- gym memberships.

2.25 An example of where this kind of pricing has already been found to be very problematic is in retail domestic energy, where over several years a variety of remedies have been implemented in response to concerns about price discrimination and its effect on the prices that customers pay. The CMA conducted a detailed market investigation into the energy market in 2016 which found that 70% of domestic customers of the six largest energy suppliers were on expensive 'default' standard variable tariffs (SVT) and could potentially save over £300 by switching to a cheaper deal.[32]

2.26 We implemented a significant package of remedies aimed at addressing these and other concerns, including a price cap for customers on prepayment meters. We discuss a number of these measures in later chapters. Further to this, a market wide price cap is due to be implemented in January 2019 following legislation introduced by the government,[33] and for that reason energy was not included in Citizen Advice's super-complaint.[34] However, in our response we draw on our thinking on the challenges in the energy market and remedies.

When is the loyalty penalty most concerning?

2.27 This section sets out our views on when the loyalty penalty is likely to raise greater or lesser concerns. We have identified four high level factors to take into account, relating to: the way in which the loyalty penalty is imposed on customers; the competitive characteristics of the market; the distributional effects of the loyalty penalty and the characteristics of the product or service affected.[35]

2.28 In summary, in our view loyalty penalty pricing is more likely to be a concern where:

- it involves confusing or misleading people, leading to poor decision making or undermines trust in markets;
- market characteristics suggest the loyalty penalty is likely to increase average prices;

[32] CMA, *Energy market investigation final report,* June 2016.
[33] See Ofgem's webpages on the default tariff cap.
[34] For more information on remedies implemented and proposed in the energy market, see chapters 6 and 8.
[35] These considerations draw on previous work carried out by the FCA. See *FCA, Price discrimination in financial services*, 2018.

- the loyalty penalty leads to harmful distributional effects;
- the product or service affected is considered ‘essential’ or constitutes a large proportion of people’s expenditure.

2.29 While there is a degree of overlap between these concerns, this classification allows us to draw out a number of key implications when considering the loyalty penalty and the different types of remedies that can be used to tackle it.

2.30 Table 2.1 summarises the key questions to consider in relation to how concerning the loyalty penalty is and when there is a greater need to act, based on these four key factors. We explain each of these considerations and questions in the rest of this section.

2.31 In Annex B we set out some initial evidence on customers’ awareness of the loyalty penalty and some of the key factors that determine whether it is likely to result in an increase in average prices in the five markets that were highlighted by Citizens Advice. We also present some summary information on the potential ‘winners and losers’ from the loyalty penalty.

Table 2.1: Key questions when considering how problematic the loyalty penalty is and when to act

Evidential question	Greater desire to act when
Does the loyalty penalty involve confusing or misleading people?	
Does the loyalty penalty pricing itself confuse or mislead people?	People lack awareness or understanding of the pricing practice which leads to poor decision making or undermines their trust or engagement in the market.
Does the loyalty penalty arise because of action by businesses to confuse or mislead, or otherwise make switching or negotiating more difficult?	Action by businesses makes it more likely that customers struggle to assess and act on the loyalty penalty
Does the loyalty penalty raise average prices?	
Does it facilitate the targeting of low prices at rivals' customers or at consumers who might otherwise not buy?	The loyalty penalty is focussed on charging very high prices to the most inactive customers rather than charging low prices to new customers.
Is competition in the market weak, and do people find it hard to choose the right deal?	Upfront competition is weaker, meaning that profits from longstanding customers are less likely to be competed away through low upfront prices.
Does the loyalty penalty lead to harmful distributional effects?	
Who is harmed?	The people paying higher prices are vulnerable in terms of the impact of higher prices or are less able to avoid the loyalty penalty.
How much are these individuals harmed?	The people who pay the high price are harmed a large amount.
How many people are harmed?	A significant group of customers is harmed.
Is the product or service essential or does it account for a large proportion of expenditure?	
Is it essential?	The product or service is considered essential.
Does the good or service constitute a large proportion of consumers' expenditure?	It comprises a large proportion of people's expenditure.

Does the loyalty penalty involve confusing or misleading people?

2.32 The loyalty penalty is of particular concern where:

- it involves businesses exploiting the difficulties people have in engaging effectively in markets, or increasing these difficulties through their own actions;[36] and
- the pricing practice misleads or confuses people or undermines their trust in markets.

[36] This point broadly relates to the idea of 'procedural fairness' used by the FCA in its recent research note: FCA, *Price discrimination in financial services: how should we deal with questions of fairness?*, 2018.

2.33 Chapter 7 sets out a number of harmful practices by businesses that make it more difficult for consumers. Chapter 6 sets out what we think can be done to give people better support to engage effectively in markets.

2.34 Loyalty penalty pricing can potentially itself cause consumers to be, or feel, confused or misled. For example:

(a) if, when signing up for a new deal, consumers are not aware of the price they are likely to pay later on, they may not make the best choice about the deals on offer;

(b) where consumers are unaware of the loyalty penalty and that they could save by switching, they may be less inclined to switch; and

(c) where consumers consider it unfair that loyal customers pay more,[37] or where they are surprised and feel 'ripped off' as a result, this can be frustrating and undermine their trust in markets. This can make them even less likely to engage in future.

2.35 Customer confusion or mistrust is therefore fundamental to consider when deciding whether to intervene directly in relation to how suppliers set their prices (as discussed in chapter 8) or in how those prices are advertised to consumers (as discussed in chapters 6 and 7). In doing so, it is also important to consider whether the ways in which businesses can implement their pricing differ in their potential to confuse customers. Price walking and legacy pricing might in some cases be harder for customers to notice and understand the effects of, than one-off price jumps after the expiry of introductory offers.

2.36 Taking both concerns into account, it is important to understand the causes of the loyalty penalty and its effect on consumer understanding and trust. Relevant evidence includes:

(a) the causes of consumers' lack of engagement, including how easy it is to avoid the loyalty penalty;

(b) the complexity of the pricing practice, and how clearly they are advertised to the customer at the point of joining the provider and each time the price increases;

(c) consumers' awareness and understanding of the loyalty penalty; and

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[37] In our qualitative research we explored perceptions of the loyalty penalty issue with vulnerable consumers and a control group of 'non-vulnerable' consumers. Many participants felt that the loyalty penalty was 'unfair' and that vulnerable consumers were likely to experience disproportionate financial harm from it - see chapter 3 for further details.

(d) how people feel about its fairness, and how it affects their levels of trust and engagement.

2.37 In summary, we believe there is a strong case for intervening where the loyalty penalty involves confusing or misleading consumers.

Is the loyalty penalty likely to increase average prices?

2.38 This section sets out some of the key factors that determine when some or all consumers are likely to be better or worse off when businesses adopt pricing that results in a loyalty penalty - rather than charging everyone the same price. There are three main mechanisms through which prices and consumer welfare can be affected by the loyalty penalty:

(a) by charging higher prices to people who are less price sensitive, the business is better off, and these people are worse off;[38]

(b) by charging some customers less than they would if everyone were charged the same price, customers who would have bought the product at the higher price are better off and may buy more of it. Some customers who would not otherwise have bought the good or service at all may now purchase it, expanding the output sold;[39] and

(c) it can trigger increased competition between businesses, as each business is better able to target customers of other businesses with a competitive price offer. Businesses may have to respond by cutting prices for their own customers to discourage customers from switching[40] – this can put downward pressure on the prices of all customers.[41]

2.39 Loyalty penalty pricing may be more likely to reduce prices overall when:

(a) businesses target price cuts at their rivals' least active customers,[42] activating and promoting competition, or at consumers who might otherwise not purchase at all. This contrasts with a situation where

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[38] In the economics literature this is described as the business appropriating some of the 'consumer surplus', ie the difference between the maximum account a consumer would be willing to pay and the price that they actually pay.
[39] For an explanation of this output expansion effect in a monopoly setting see OFT, *The economics of online personalised pricing*, 2013, chapter 3.
[40] Although we note this incentive may sometimes be diluted in some markets. For more discussion see Ofcom, *Strategic review of consumer switching*, 2010.
[41] For an explanation of this 'intensification of competition effect' see OFT, *The economics of online personalised pricing*, 2013, chapter 3.
[42] This captures the idea of 'best response asymmetry', where each business finds their rivals' customers difficult to win and target price cuts at them – this pattern, of one supplier's 'strong' market being its rival's 'weak' market and vice versa, is associated with a greater likelihood that price discrimination is positive overall. For more explanation see OFT, *The economics of online personalised pricing*, 2013, section 4a.

suppliers primarily use it to segment more strongly within their own set of loyal customers, to charge the highest prices to those least likely to switch;[43]

(b) the profits that businesses make on consumers later in their tenure are competed away through fierce competition to win the customer in the first place (the 'waterbed effect'); and

(c) customers typically periodically search and switch, rather than there being distinct groups of customers who more consistently do or do not engage.[44] This is because where the same group of customers always engage, businesses will not have a strong incentive to attract these customers as they will switch again if the price rises in the future. In contrast, where most customers periodically engage with the market, suppliers will have an incentive to set a low initial price to attract these customers as they can charge them higher prices in subsequent periods before they switch again.[45]

2.40 Price differences also mean that consumers gain when they switch provider or negotiate. This motivates and compensates consumers for the effort involved in searching, switching, and negotiating.[46] Without this there may be more limited competition between businesses.

2.41 It is possible that under certain circumstances the effect on competition could be so strong that the prices paid by less active customers are also lower than a uniform price would be.[47] On the other hand, where competition between businesses to attract new consumers is weak, the loyalty penalty is more likely to lead to an overall increase in average prices.

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[43] Price discrimination may not increase overall competition, if businesses are simply segmenting their strong group of consumers (those that have already purchased from them) into two subgroups: a very strong group and a strong group. In this case, it reduces consumer surplus. See Shin, J. and Sudhir, K., *A customer management dilemma: When is it profitable to reward one's own customers?. Marketing Science, 29(4)*, pp 671-689, 2010.
[44] There are also distributional considerations, since in the case where all customers engage periodically we would expect more customers to benefit from the low price at least some of the time, whereas when there are distinct groups of consumers it will always be the same customers who pay the low price and the same ones that pay the high price.
[45] See for example Klemperer, P. *Markets with consumer switching costs*, Quarterly Journal of Economics 102, pp 375-394, 1987.
[46] Research in relation to domestic energy consistently finds monetary savings to be a key driver of switching. See for example: Deller, D et al. *Switching energy suppliers: it's not all about the money*, CCP working paper pp 17-5, 2017.
[47] For more explanation see OFT, *The economics of online personalised pricing*, 2013, chapter 3. and (for example) Corts, K. *Third-Degree Price Discrimination in Oligopoly: All-Out Competition and Strategic Commitment*, Rand Journal of Economics, 29(2), pp 306–323, 1998.

2.42 In assessing whether the loyalty penalty leads to higher average prices, it is therefore important to collect evidence on whether:

- businesses are using the pricing mechanism to target their rivals' customers and win new business, or are instead using it to segment strongly within their own set of loyal customers;
- there is intense competition for active customers in the market concerned or not; and
- many customers typically periodically search and switch, or there are distinct groups, where some customers switch frequently but others do not.

2.43 These factors should inform not only the assessment of whether the loyalty penalty is problematic, but also the design of any remedy to deal with it.

2.44 Some initial information on the characteristics of the five markets highlighted by Citizens Advice is presented in Annex B, but further work is required to develop this evidence base. This will a key part of the ongoing work by Ofcom and FCA in these markets (see Annexes C and D).

Is the loyalty penalty likely to have harmful distributional effects?

2.45 The discussion in the previous section highlights that the loyalty penalty can create winners and losers – any intervention that directly limits the extent of the loyalty penalty may similarly create winners and losers. This section discusses when and why we may be concerned about who wins and who loses. In this discussion we have drawn on the framework that the FCA recently set out for approaching the fairness of price discrimination.[48]

2.46 In determining whether to act on distributional grounds the key questions to consider are who is harmed and how big is the harm.

Who is harmed by the loyalty penalty?

2.47 We will be more concerned about the distributional effects where it involves consumers who are vulnerable paying more, and those who are not vulnerable paying less.[49] This would it involve higher prices for customers

[48] FCA, *Price discrimination in financial services: how should we deal with questions of fairness?*, 2018. Note that the FCA has asked for comment on this draft framework; it has not consulted on its formal adoption.
[49] Note that this in addition to the concerns embodied in The Equality Act 2010 which prohibits, with a few exceptions, discrimination on the basis of protected characteristics such as age, disability, pregnancy, gender or sex related issues, marital status, race or religion.

who are particularly likely to be harmed by paying a high price, or at high risk of being unable to engage effectively in a market to get a good deal.

2.48 Chapter 3 discusses the nature of consumer vulnerability and why vulnerable consumers may be more at risk of experiencing a loyalty penalty, and chapter 4 considers the impact of the loyalty penalty on consumers, and whether vulnerable consumers are more likely to pay it.

2.49 There may be other circumstances in which consumers (even if they are not vulnerable) struggle to avoid the loyalty penalty. There can be situations where customers become locked in to a particular provider or have very limited options regarding the providers they can use, for example 'mortgage prisoners' who cannot switch providers because of changes in lenders' eligibility criteria over time, or those living in areas with mobile coverage from only one provider.

2.50 More generally, when deciding whether to act or what actions might be necessary to address the loyalty penalty, we may wish to take account of the extent to which consumers are able to avoid the loyalty penalty. For example, we may consider that it is more appropriate to act where:[50]

- customers are not aware of the existence of the loyalty penalty or that they are paying it; or
- customers are unable, or find it particularly difficult, to avoid the loyalty penalty, where those that find it hard to switch do not have the option of choosing not to consume the product at all.

2.51 In markets where those who pay high prices tend to be vulnerable and those who pay low prices tend not to be, it may be desirable to limit the high prices even if it means that the low prices might go up. In markets where vulnerable consumers sit in both groups, it may be appropriate to target protections on vulnerable groups paying more, in order to reduce the extent of increases for those paying lower prices.

2.52 The initial information we have gathered on the five markets identified by Citizens Advice suggests that customers with long tenure include those that are likely to be vulnerable, although there is also evidence that in some markets vulnerable customers may also be among those that may benefit from the current pricing practices.

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[50] These factors have recently been highlighted by the FCA in its Discussion Paper on fair pricing in financial services.

How big is the harm to those affected?

2.53 In considering whether it is appropriate to take action to address the loyalty penalty or its impact, the extent of the harm to those affected will be relevant.

2.54 The extent of the harm has two dimensions – how many people are harmed and how much they are harmed. Taking action to tackle the loyalty penalty will be more desirable when there is either a large number of customers harmed by it, or when the amount of harm to each affected customer is large. It is more desirable to take action where the harm to those affected is large relative to the benefits to those that gain from the loyalty penalty.

2.55 In assessing the scale of harm from the loyalty penalty, it is important to have a meaningful benchmark in mind. While a comparison between the high and low prices on offer is informative, it is likely that the low prices would increase if businesses were required to offer everyone the same price.

2.56 It is also important to make sure that comparisons are on a like-for-like basis controlling for any variation across customers in the costs of serving them. These issues, along with the kind of empirical evidence that is relevant to assessing the size and incidence of harm, is explored in more detail in chapter 4.

Is the product or service affected 'essential'?

2.57 A final set of considerations in assessing to what extent loyalty penalty pricing is a concern relates to the characteristics of the product or service affected, and in particular whether it can be considered 'essential'.

2.58 Essential services refer to services that consumers need to participate in society and the economy, and where significant harm might arise if consumers are not able to access the service. There are likely to be high levels of public concern where loyalty penalty pricing is applied to essential services, as consumers typically have little choice but to use such services.

2.59 Several of the markets that are identified in the super-complaint could be considered essential against this criterion. In telecoms, for example, mobile and broadband are seen as essential as consumers use these services as the means to contact the emergency services, keep in touch with family and friends, or provide access to information, education and entertainment.[51] Some insurance products will be essential. For example, motor insurance is a legal requirement for anyone who owns or drives a vehicle, and it is a

[51] Ofcom, *Affordability of communications services essential for participation: quantitative research*, July 2014.

standard condition of mortgage agreements that the owner has to have buildings insurance in place.

2.60 While recognising that this is an important consideration, we have not focussed exclusively on essential services in our response. Many of the practices that we identify in chapter 7, for example, occur across the economy, leading to substantial consumer harm. Other product characteristics are also relevant in assessing concerns about the loyalty penalty. For example, we are likely to be particularly concerned where a good or service comprises a relatively high proportion of a consumer's expenditure.

Conclusion

2.61 This chapter has explained what the loyalty penalty is, the causes underlying it, and some factors that should be taken into account in considering whether the loyalty penalty raises greater or lesser concerns.

2.62 The loyalty penalty arises because some consumers are less likely to switch or negotiate, and businesses often choose to charge these consumers more. There are a number of reasons why some consumers are more likely or able to engage in markets relating to features of the market, behaviours and characteristics of consumers and behaviour by businesses.

2.63 The impact of the loyalty penalty on the prices that consumers pay will not always be harmful - it can lead to lower average prices and higher consumer welfare – but it creates losers as well as winners.

2.64 We will be particularly concerned about the loyalty penalty where:

- it involves suppliers confusing or misleading customers, exploiting difficulties people have in engaging effectively in markets, or increasing these difficulties through their own actions, including through the pricing practice itself. We think that price walking and legacy pricing might be particularly difficult for customers to assess and act upon;

- market characteristics suggest the ability of businesses to charge different prices to different customers based on loyalty is likely to increase average prices. This is less likely to be the case where it helps suppliers to target price reductions at their rivals' least active customers or at new customers. It is more likely to be the case when weak upfront competition means that the profits from high price customers are not fully competed away through low prices for new customers and there are distinct groups of customers who do and do not engage;

- it leads to harmful distributional effects. We will be particularly concerned where those paying higher prices are vulnerable, where they are unable to act to avoid the loyalty penalty or are not aware of it. Concerns about distributional effects will be greater where either many people are affected or those that are affected are paying a very high price;

- the product or service affected is considered essential or constitutes a large proportion of people's expenditure.

2.65 Interventions that remove barriers to switching and negotiating and address harmful business practices will help reduce the number of people affected and drive more effective competition for the benefit of all consumers. These have significant benefits across the board. However, in some cases these will not reach all consumers, so regulators should also look at targeted pricing interventions.

2.66 Pricing interventions that directly limit the prices that customers pay, are likely to create both winners and losers, and depending on the characteristics of the market and the intervention chosen, risk leading to higher average prices. It is therefore important to collect evidence on those market characteristics, and to build a detailed understanding of the likely winners and losers from any intervention. We explore the challenges faced by vulnerable consumers and who is impacted by the loyalty penalty further in the next two chapters.

3. Vulnerable consumers

- Many consumers can be vulnerable at certain times and in certain markets.
- However, some individuals also have certain characteristics that can lead to greater risks of experiencing problems across a range of markets. These include being on a low income, being elderly, having physical disabilities or mental health problems, among others.
- Many such individuals can face additional challenges in switching or negotiating with suppliers, including psychological and cognitive barriers, accessibility barriers, low financial resilience, and time pressures; and therefore may need additional support.
- Most participants in our qualitative research were aware of the loyalty penalty and felt it was unfair and hit vulnerable consumers hardest.

Introduction

3.1 In its super-complaint, Citizens Advice stated that certain subsets of consumers who can be considered vulnerable are likely to struggle with shopping around and switching. They are also likely to experience the financial impact of the loyalty penalty disproportionately where it arises.[52]

3.2 Throughout our response, we have given particular consideration to vulnerable consumers' experience of the loyalty penalty. This chapter is structured as follows:

(a) what we mean by consumer vulnerability, including a consideration of the regulators' approach to vulnerability in the five markets;

(b) the cross-cutting challenges that vulnerable consumers can face in markets when getting deals, including barriers to switching and negotiating; and

(c) vulnerable consumers' awareness and perceptions of the loyalty penalty.

3.3 We have drawn on a range of sources. This includes our programme of work on vulnerable consumers which was launched earlier in 2018.[53] This work has comprised wide-ranging stakeholder engagement, evidence gathering and

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[52] Citizens Advice, *Excessive prices for disengaged consumers: a super-complaint to the Competition and Markets Authority*, 2018, chapter 2.
[53] The CMA's 2018/19 Annual Plan identified a priority focus on vulnerable consumers, which has continued in the draft 2019/20 Annual Plan (under consultation at the time of writing).

analysis to understand the different dimensions of consumer vulnerability across markets and considered how the CMA can help. We will be publishing our findings in a separate paper in early 2019.[54]

3.4 We have also drawn on qualitative research that we commissioned from BritainThinks with people who are on low incomes, have poor mental health or a physical disability or are elderly. The aim of the research was to provide an understanding of the challenges which such individuals can face across a range of markets - including mobile, broadband and insurance - and identify what support may help to address these. We refer to the research findings throughout this response.[55]

3.5 We consider whether vulnerable consumers are more likely to pay a loyalty penalty in the five markets, in chapter 4.

What is consumer vulnerability?

3.6 In a broad sense, consumer vulnerability can refer to any situation in which an individual may be unable to engage effectively in a market and as a result, is at a particularly high risk of getting a poor deal.

3.7 Anyone can be vulnerable in a specific context or market such as when going through a difficult period in their lives, for example a bereavement. We have considered the impact of bereavement on market engagement further in our recent market study into funerals.[56] Vulnerability can also arise if a market is particularly complex and it is difficult to understand the options available - such as in certain digital or financial services markets.

3.8 Individuals with certain characteristics can be at risk of facing particularly severe, persistent problems across markets. Our qualitative research focussed on four such characteristics - age, low income, physical disability and mental health problems. This is not a definitive list of characteristics that are likely to be associated with vulnerability; others include: low levels of education; being time-poor; indebtedness; English as a second language;

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[54] Further detail on the CMA's programme of work on vulnerable consumers, including summaries of roundtable discussions on different aspects of vulnerability, is available on our vulnerable consumers webpage. See BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018.
[55] In September 2018 we commissioned BritainThinks, an independent research agency, to conduct qualitative research comprising 49 face-to-face depth interviews, two-day ethnographic interviews and online activities, with consumers who may be considered vulnerable because they are on low incomes (defined as less than 60% of median income). Across the sample, participants also had other vulnerabilities, such as having mental health problems, a physical disability, or being elderly. The research explored participant's experiences across multiple markets, including telecoms (mobile, broadband, fixed line telephone and pay TV), insurance (home and motor) and energy. The full research findings are available in the published report by BritainThinks, available on the CMA vulnerable consumers webpage; chapter 6 considers awareness and experiences of the loyalty penalty.
[56] CMA, *Funerals market study: interim report and consultation*, 29 November 2018.

lacking skills or confidence online; being digitally excluded; or living in social isolation or a remote geographical area. For ease of reference, we use the general term 'vulnerable consumers' in our response to refer to people with at least one of these characteristics.[57]

3.9 Not all individuals with such characteristics are necessarily vulnerable, or vulnerable in the same way. For example, taking age: individuals aged 65 to 74 have the highest level of net financial wealth compared to all other age groups.[58] In our qualitative research, elderly participants tended to have the most 'thought out' approaches to money management, such as filing systems for old and new bills. In addition, most participants on a low income[59] had taken some kind of action to switch, shop around or negotiate a better deal.[60]

3.10 We also recognise that many individuals with characteristics associated with vulnerability do not self-identify as 'vulnerable' or want to be labelled as such.[61] Their behaviour and level of engagement can also vary across markets. Vulnerability is therefore not a binary concept; it is multidimensional and often highly context specific. Some characteristics are also correlated with each other, such as problem debt and mental health problems.[62]

3.11 Throughout our response, we have given particular consideration to the four subsets of consumers identified as vulnerable by Citizens Advice in its super-complaint, as well as physical disability which we explored in our research.

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[57] We note that vulnerability has a specific meaning within the context of the Consumer Protection from Unfair Trading Regulations 2008 (CPRs), which apply a particular definition of vulnerability to determine when a trader may have breached consumer law protections for a 'vulnerable group of consumers'. Under this definition, consumers may be vulnerable due to 'a mental or physical infirmity, age or credulity'. See OFT, *Consumer protection from unfair trading guidance on the UK regulations*, 2008. In chapter 7 of this response, where we consider whether business practices may be in breach of consumer law, we apply this definition of vulnerability.
[58] ONS, *Summary of net financial wealth banded by age,* released 23 October 2018.
[59] Defined as below 60% of median income.
[60] Other research has similarly found variation in shopping around among different groups of vulnerable consumers. For example, the FCA found that unemployed renters and those with low credit scores had a tendency to shop around in home insurance. Source: FCA, *Pricing practices in the retail general insurance sector: household insurance*, 31 October 2018.
[61] In our qualitative research, many participants, all of whom were on a low income, did not see themselves as vulnerable.
[62] For example, half of people in problem debt also have mental health problems and people with problem debt are twice as likely to develop major depression than those not in debt. Mental health problems are also correlated with financial difficulty - a quarter of British adults with a mental health problem are in problem debt. Source: Money and Mental Health Policy Institute, *Money and mental health: the facts*, June 2017.

Key statistics on groups of vulnerable consumers considered in our research

- Elderly people, defined as those aged 65 or over. Close to a fifth (18%) of the UK population fall into this group, equivalent to around 12 million people.[63] Elderly consumers can have other characteristics associated with vulnerability. For example, the prevalence of certain health conditions, such as dementia, can increase with age.[64]

- Individuals on low incomes, defined as income below 60% of the median. Just over a fifth (22%) of the UK population (around 14 million people) live in low income households.[65]

- People with mental health problems. There are a wide range of mental health conditions with varying levels of severity - from depression to affective psychoses to schizophrenia. A quarter of the population in England experience a mental health problem each year[66] and one in six report experiencing a common mental health problem (such as anxiety or depression) in any given week.[67] People experiencing mental health problems are less likely to be in paid employment (43% vs 74% of the general population and 65% with other health conditions) and more likely to be in low pay, high turnover, temporary or part-time work.[68]

- Individuals with low levels of education. Just under 30% of the UK population have educational qualifications below NVQ level three (equivalent to two A levels) and 8% of the UK population aged 16 to 64 have no educational qualifications (close to four million people).[69]

- People with physical disabilities. Just over a fifth (22%) of the UK population (around 14 million people) report having some form of disability.[70]

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63 ONS, *Overview of the UK population,* July 2017.
64 For example see Alzheimer's Society, *Dementia UK: second edition*, 2014.
65 ONS, *Family resources survey*, 2017. Survey of 19,000 UK households. This figure is calculated after housing costs are taken into account.
66 Adult psychiatric morbidity survey, 2007. This is the main national survey of health and wellbeing in England, which takes approx. 7,000 adults through clinical screeners for mental health problems once every seven years).
67 Mental health and wellbeing in England: adult psychiatric morbidity survey, 2014.
68 Money and Mental Health Policy Institute, *Money and mental health: the facts*, June 2017.
69 Annual Population Survey (from Nomis), covering January 2017 to December 2017.
70 DWP, *Family resources survey 2016/17*, 2018. Estimate is based on ONS Family resources survey data and draws on the definition of having a longstanding illness, disability or impairment which causes substantial difficulty with day-to-day activities.

Regulator approaches to vulnerability

3.12 The regulators for the five markets identified in the super-complaint - Ofcom and the FCA - actively consider vulnerable consumers in their work. As public bodies, both regulators are also subject to the Public Sector Equality Duty under the Equality Act 2010.[71]

Ofcom

3.13 Ofcom has a statutory duty to consider the needs of consumers with disabilities, or who are elderly, or on low incomes.[72] It has rules which require communications providers to take into account certain characteristics when giving consideration to vulnerable consumers, namely ‘age, physical or learning disability, physical or mental illness, low literacy, communications difficulties or changes in circumstances, such as bereavement’. Under Ofcom’s rules, regulated providers must establish, publish and comply with clear and effective policies and procedures for the fair and appropriate treatment of consumers whose circumstances may make them vulnerable.

3.14 Ofcom’s 2017 ‘Access and inclusion’ report examined the take up and use of communications services by vulnerable consumers.[73] The next report, due to be published in January 2019, will update many of the metrics from the 2017 report (including disability research), and include a section on consumer engagement.

3.15 Separately, Ofcom has recently launched a review into price differentiation in the fixed broadband market, with a focus on vulnerable consumers (see Annex C for more detail).

The FCA

3.16 The FCA has an operational objective to secure an appropriate degree of protection for people in financial markets. It identifies four key drivers that could lead to consumers being ‘potentially vulnerable’, related to: low financial resilience; a recent life event such as a divorce; low financial capability or a health issue that affects day-to-day activities a lot. The FCA defines a vulnerable consumer as ‘someone who, due to their personal circumstances

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[71] The Public Sector Equality Duty requires public bodies to have due regard to the need to eliminate discrimination, advance equality of opportunity and foster good relations between people who share a protected characteristic and those who do not, when carrying out their activities.
[72] Ofcom’s statutory duties are set out under the Communications Act 2003. Ofcom introduced new general conditions (C5.2-5.5), effective from 1 October 2018, that aim to ensure that communications providers give sufficient consideration to the particular needs of people with disabilities and people whose circumstances may make them vulnerable.
[73] Ofcom, *Access and inclusion report*, March 2017.

is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care'.[74]

3.17 The FCA consulted on and published its 'Approach to consumers' in July 2018 as well as a Discussion Paper on the case for introducing a duty of care.[75] The FCA will consult on guidance for firms on the identification and treatment of vulnerable consumers in early 2019. The guidance will seek to provide clarity of its expectations on firms and ensure good outcomes for all consumers, particularly vulnerable consumers.

3.18 While there are commonalities in these approaches to understanding consumer vulnerability - such as vulnerability being related to personal circumstances - there are also differences in emphasis and focus. In chapter 4 we consider differences in data collection by regulators across markets on the different indicators of vulnerability.

What additional challenges do vulnerable consumers face?

3.19 Vulnerable consumers can experience additional challenges in searching, switching and negotiating with suppliers to get a good deal, compared to those faced by consumers generally. We recognise that not all vulnerable consumers will necessarily experience challenges, and that for those who do, the nature and extent of these challenges will vary for each individual depending on their vulnerability, or the interaction between multiple vulnerabilities. Nonetheless, it is possible to identify some common challenges, which we consider briefly here. We will be exploring these challenges in detail in a forthcoming paper on vulnerable consumers.

3.20 We also recognise that there are a range of unacceptable practices which some suppliers use to hinder consumers from engaging, switching or getting a better deal. Such practices can have a particularly negative impact on individuals who may be vulnerable. We consider this further in chapter 7.

Psychological and cognitive barriers

3.21 Some vulnerable consumers may choose not to switch supplier or to negotiate with an existing supplier, due to a fear or aversion to change. For

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[74] FCA, *Approach to consumers*, July 2018. In this document the FCA sets out how it considers vulnerable consumers as a regulator. The FCA Mission states that understanding vulnerability is central to how the FCA makes decisions. It states that consumers in vulnerable circumstances are more susceptible to harm and generally less able to advance their own interests. The FCA Mission makes clear that the FCA will prioritise consumers who are unable to shop around over consumers who can shop around but choose not to do so. For example, the FCA will prioritise consumers who are vulnerable because they cannot exit an existing contract or have a restricted choice of alternative providers.
[75] FCA, *A duty of care and potential alternative approaches*, 17 July 2018.

example, people with mental health problems such as stress, anxiety or depression, may avoid switching because they require stability and routine to help maintain their mental wellbeing, and change can be highly disruptive.[76]

3.22 In some cases, vulnerable consumers may lack the necessary cognitive skills to carry out activities such as comparing prices, particularly in highly complex markets (such as where there are bundled products such as in broadband or compounding effects such as in mortgages or cash savings).

3.23 For example, people with dementia (which elderly consumers are more at risk of developing) are often less able to assess and remember complex information and make accurate decisions. Normal cognitive ageing can also mean that elderly people find it more difficult (or need more time) to deal with complex[77] or unfamiliar decisions, such as changing insurance provider.[78] Some mental health conditions can also impair cognitive skills. For example, individuals with depression or borderline personality disorder can experience attention problems.[79]

> I'm not quite as sharp as I used to be … My vocabulary used to be much bigger.
> Qualitative research participant, long term health condition, aged 75+, Nottingham.
>
> The thoughts in my head, the mental health they make my life hectic … I am rubbish with money and I'm useless at organisation.
> Qualitative research participant, mental health problems, aged 35-44, Watford.

3.24 Some vulnerable consumers can also struggle with money management and financial capability. In our qualitative research, younger participants without a degree were less likely to feel confident in their ability to manage money and finances, or in their ability to get a good deal for products and services. Similarly, Citizens Advice presented evidence in its super-complaint that individuals without a degree perform less well in complex tasks than those with a degree.[80] People with particular mental health conditions such as ADHD or bipolar disorder can also struggle with financial management.[81]

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[76] Citizens Advice, *Essential service markets and people with mental health problems*, 2018.
[77] Alzheimer's Society, *What is dementia? Factsheet*, January 2017.
[78] The big window, *The aging population: aging mind literature review report*, 2017 and The big window, *The aging population: coping mechanisms and third party access*, 2017.
[79] Money and Mental Health Policy Institute, *Seeing through the fog*, February 2017.
[80] Citizens Advice, *Excessive prices for disengaged consumers: a super-complaint to the Competition and Markets Authority*, 2018, page 26.
[81] Money and Mental Health Policy Institute, *Seeing through the fog*, February 2017.

> I'm not confident with my money … I do try and budget but it never works. When I've got less money I find I budget better. A bit more money and I find I end up throwing money at things I don't need.
>
> Qualitative research participant, mental health problems, aged 35-44, Glasgow.

Accessibility barriers

3.25 Vulnerable consumers may lose out on deals because they do not have adequate skills or the confidence to engage in activities online, such as using price comparison websites (PCWs) to compare suppliers or are digitally excluded and so do not have access to the internet and online deals. For example, Ofcom found that the proportion of adults in socio-economic group DE households (semi-skilled and unskilled occupations and the unemployed) who do not go online is almost double the UK average (22% vs 12%), and that just under half (47%) of people aged 75+ do not use the internet.[82]

> I'm not too sure about that [online banking]. It's alright for you young people but I'm very cagey about it and [bank X] is only a mile and a half up the road.
>
> Qualitative research participant, long term health condition, aged 75+, Glasgow.
>
> I prefer not to use the internet. I never learned how to use a computer properly. I find it difficult. I'm not built that way.
>
> Qualitative research participant, mental health problem, aged 45-54, Watford.

3.26 Lack of access to key enabling products, such as a car or a bank account, can also be a barrier to vulnerable consumers getting a good deal: 62% of individuals without a bank account have an income of less than £15,000.[83]

3.27 Vulnerable consumers can also struggle to communicate with suppliers through particular channels. This can mean that they disengage from their service and may become more likely to auto-renew or roll over their contract. For example, individuals with mental health problems often have serious difficulties engaging via at least one commonly used communication channel such as telephone, face-to-face contact, or postal letters.[84] Conversely, older people tend to prefer face-to-face or telephone contact and may struggle to

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[82] Ofcom, *Adults' media use and attitudes report,* 2018.
[83] FCA, *The financial lives of consumers across the UK: key findings from the FCA's Financial Lives Survey 2017*, June 2018.
[84] Money and Mental Health Policy Institute, *Access essentials*, July 2018.

use digital communication channels such as email or Skype due to a lack of digital skills and/or internet access.[85]

> If I get letters they just go in the bin, I don't [read] anything. I don't like to pick up the phone. I just want to shut everything out and be alone in my room.
> Qualitative research participant, mental health problem, aged 35-44, Glasgow.

3.28 People may be vulnerable because they are isolated geographically and/or socially. This can act as a barrier to their ability to switch suppliers. For example, qualitative research participants who were living in particularly remote rural areas reported that in some markets, such as broadband, they had a limited number of suppliers to choose from - in some cases, only one.

> One elderly participant who lived in a very rural area and had a very small social network, had not switched her energy provider for 20 years - partly because she trusted them to provide a good service, but also because her relative isolation meant she had very limited knowledge of the ability to, and benefits of, switching.

Low financial resilience

3.29 Financial resilience refers to an individual or household's ability to withstand unforeseen life events which can have an impact on finances - for example, being made redundant or being diagnosed with a long term health condition. Therefore, having low financial resilience can also be a barrier to vulnerable consumers being able to shop around or switch suppliers. It can mean that the impact of something going wrong, or of paying a loyalty penalty, causes greater financial harm to vulnerable consumers than to consumers generally.

> All you need is something to go wrong with the house or something to go wrong with the car and then you're not ticking over anymore.
> Qualitative research participant, physical disability, aged 45-54, Watford.

3.30 Fear of the risk of something going wrong as a result of changing suppliers was a recurring theme in our qualitative research. Participants on low incomes often chose to stay with their existing provider because they wanted reliability and continuity of service and feared being disconnected. For some participants, aversion to the risks arising from constrained finances sometimes meant that they were unwilling to switch for fear that something

[85] For example, see Age UK, *Later life in a digital world*, December 2015.

would go wrong or that contractual arrangements would result in them being penalised. In cases where participants had had previous debts written off by suppliers, there was a fear that they may be charged more or lose out on certain tariffs with new suppliers.[86]

> Say you moved from [supplier X, supplier Y], whatever, to another supplier, you've no idea if you've got, like, say 12 months contract rolling 18 months, two years, 20 years, I don't know. You don't know if there'll be any, sort of, fines for moving to another supplier. Not a clue.
> Qualitative research participant, physical disability, aged 75+, Rhyl.
>
> I think they're [energy supplier] expensive but I think that I'm stuck. I've heard that you lose your Warm Home Discount if you switch, you've got to start from scratch with claiming it again and you can lose out on it, and if you've got any credit left [on your prepayment meter] when you switch, you don't get it back. It's catch 22. Switching would just be another thing to battle with.
> Qualitative research participant, low income, aged 25-34, Watford.

Time pressures

3.31 As we explore in more detail in chapter 7, switching suppliers or negotiating a better deal with an existing supplier can involve significant 'hassle' and time costs. In the case of vulnerable consumers, these barriers to accessing better deals can be exacerbated to the point where it is no longer an option.

> One research participant said that as the carer for her six year old son, she was concerned about being on the phone for longer than 15 minutes at a time, in case her son's school contacted her to administer emergency medication. She could not afford another phone and the school was not insured to store the medication onsite.
>
> 'I have to be available within 15 minutes so I'm always on a time limit and I can never go very far while he's at school.'

3.32 As a result of the different types of challenges that they can face, vulnerable consumers may require additional support to engage effectively in markets. This could be in the form of family, friends, or third party intermediaries, as well as suppliers. A number of research participants described that they were reliant on others to support them when engaging with markets. A lack of such

[86] For further detail, see BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018.

support can therefore act as a barrier to engagement. We consider the role of intermediaries in more detail in chapter 6.

> One research participant who suffered from alcohol dependency explained that he was reliant on his long term girlfriend to help with financial management for the household. His daughter also helped him financially when needed.
>
> 'I'm not so confident managing money. I'd forget about things, my girlfriend keeps me on track. The best way is for her to manage it. My daughter helps out, she'll pay towards the bills.'

What do vulnerable consumers think about the loyalty penalty?

3.33 We explored the concept of the loyalty penalty with participants in our qualitative research.[87] We recognise that the views presented are not necessarily representative of vulnerable consumers generally (which, as highlighted earlier, are not a homogenous group), and only of the sample of individuals we spoke to. Nonetheless, it has provided us with some interesting insights.

3.34 At least half of participants spontaneously raised the loyalty penalty issue during interviews, and the majority recognised the concept when prompted, and said that they were unsurprised by it.[88] The minority of participants who were surprised by the idea of a loyalty penalty tended to be isolated or digitally excluded, have mental health problems or low levels of education. These groups often found the topic of shopping around and switching in general to be complicated and sometimes overwhelming.

> Newer customers get good deals … [provider X] often have offers I'm not eligible for. That's how they get their customers. But they shouldn't hide it in the small print, things like the fact that your tariff often doubles after six months …
> Qualitative research participant, physical disability, aged 75+, Watford.
>
> They [longstanding customers] definitely pay more. Every single offer you see is always for new customers.
> Qualitative research participant, physical disability, aged 18-24, London.

[87] BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018, chapter 6.
[88] Awareness among participants may have been influenced by media coverage of the loyalty penalty issue while the research fieldwork was being conducted.

3.35 Most participants felt the loyalty penalty was unfair. For many, this was due to a sense that being a longstanding customer was a positive, and something that should be rewarded as a matter of principle.

> I hope that longstanding customers pay less. I've been with [provider X] for a long time, I would expect a good deal.
> Qualitative research participant, mental health problems, aged 35-44, Nottingham.

3.36 Most participants also expected vulnerable consumers to be more likely to pay a loyalty penalty. This was linked to the view that to get a better deal and avoid paying a loyalty penalty requires consumers to do all of the ‘work’ to switch, shop around and negotiate - which vulnerable consumers can find more difficult. For several participants, this was reflective of a broader perception that life is particularly hard and unfair for vulnerable consumers. The fact that vulnerable consumers may suffer greater financial harm from paying a loyalty penalty, was also considered unfair.

> It's not fair … especially if you're ill as well - all this running around and then the thought of having to do it all again next year would just be horrendous … They should offer deals to existing customers.
> Qualitative research participant, physical disability, aged 45-54, Watford.
>
> Your higher earners are not as worried about if they're paying a couple of pounds extra each month because they can afford it.
> Qualitative research participant, physical disability, aged 45-54, Watford.

Conclusion

3.37 This chapter has set out our understanding of vulnerability, with a particular focus on the four groups which Citizens Advice identified in its super-complaint - those on low incomes, with mental health problems, low levels of education, and the elderly.

3.38 Such individuals can face additional challenges when searching, switching and negotiating with suppliers. As a result, they may be more likely to pay a loyalty penalty where it arises. We explore this in further detail in chapter 4.

3.39 We have also considered awareness and perceptions of the loyalty penalty issue among vulnerable consumers in our qualitative research. While these views are not necessarily representative of a wider population, they provide interesting insights - the loyalty penalty is considered unfair, and to be disproportionately harmful to vulnerable consumers for whom the financial impacts of a loyalty penalty can be greater.

4. How big is the loyalty penalty and who pays it?

- Existing estimates suggest there is a substantial loyalty penalty paid by consumers each year in each of the five markets identified by Citizens Advice, and this penalty may be around £4 billion in total across the five markets.
- Markets differ significantly in terms of the average penalty paid by customers and the number of people who could be affected, ranging from under one million people in mortgages to over 12 million in home insurance.
- The estimates we have reviewed have some limitations and estimates from different sources can arrive at materially different numbers. This highlights the importance of using robust methodologies and data. Estimates with the biggest gaps are in mobile, broadband and home insurance, and work is already underway by regulators to address this.
- Better data on which consumer groups pay the highest loyalty penalty is required. There is limited evidence on the extent to which vulnerable consumers are paying a loyalty penalty and on whether the same consumers are paying a loyalty penalty across different markets.
- To address this gap, we recommend that regulators assess the feasibility of a data matching exercise to identify the size of the loyalty penalty and who pays it across markets.
- Regulators should also publish informative and simple metrics on the loyalty penalty on a regular basis, in key markets and for each supplier.

Introduction

4.1 As set out in chapter 2, concerns about the loyalty penalty are greater where: the difference in prices paid by longstanding and new customers is large, where many consumers pay this price difference, and where groups of vulnerable consumers are particularly affected. In such cases, regulators may consider that stronger action is justified.

4.2 This chapter assesses the available evidence on the size of the loyalty penalty across the markets identified by Citizens Advice, and who pays it. It is structured as follows:

(a) the size of the loyalty penalty in the five markets based on different available estimates;

(b) the evidence on who pays the loyalty penalty, and in particular whether vulnerable consumers are more likely to pay it;

(c) filling gaps in the evidence base on the size and who pays the loyalty penalty;

(d) regular publication of estimates of the loyalty penalty; and

(e) recommendations on measuring and publishing estimates of the loyalty penalty.

Size of the loyalty penalty

4.3 Table 4.1 summarises the available estimates of the loyalty penalty in the five markets identified in the super-complaint. These estimates show that in each market, there appears to be a substantial loyalty penalty paid by consumers each year. This penalty is around £4 billion in total across the five markets: nearly £1 billion in broadband and £0.3 billion in mobile (for handset inclusive contracts); £1.1 billion in savings accounts; £0.7 billion in home insurance and £0.8 billion in mortgages, based on the estimates in bold in Table 4.1.

4.4 Table 4.1 also shows that the markets differ significantly in terms of the number of people affected and the average loyalty penalty paid by customers or households. On one end of the spectrum, in home insurance the annual average loyalty penalty per person is relatively small in absolute terms (£57), although it can be significant relative to the average insurance premium and is higher for people who stay with their provider for a long time. But it could be paid by over 10 million households.

4.5 In contrast, in mortgages, the loyalty penalty affects a relatively small number (0.8 million)[89] and proportion of consumers, but the average loyalty penalty those consumers pay (£1,000) is particularly high when compared to other markets, due to the large financial size of mortgages. This can have implications for interventions considered by regulators (for example how targeted those interventions should be).[90]

[89] This is because of high levels of consumer engagement in this market: three-quarters of consumers switch to a new mortgage deal within six months of moving onto a reversion rate. See FCA, *Mortgages market study interim report,* May 2018, paragraph 1.13.

[90] As a consumer may pay a penalty in more than one market, it is not possible to determine from the various estimates the total number of people who pay a loyalty penalty in the markets we looked at altogether. However, the consumer survey by Citizens Advice, which covered all five markets, suggests that eight in 10 people responsible for household bills are paying the loyalty penalty at least in one of these markets.

4.6 While these estimates are indicative of the relative size of the issue in different markets, there are some gaps in the evidence, as discussed in paragraphs 4.29 to 4.32.

4.7 It is important to note that estimates of the loyalty penalty are measures of difference between the price paid by longstanding customers and new customers for similar goods.[91] These differences represent the potential saving that individual longstanding customers might currently make if they switched to another deal.[92] They do not represent the total saving that would result if the gap between prices charged to longstanding and new customers were reduced. This is because if providers were required to reduce this gap, then the price charged to new customers would likely be higher than the current new customer price (which would in turn reduce the potential savings available to longstanding customers).[93,94]

4.8 As a result, the loyalty penalty estimates we present should not be interpreted as a measure of the extent to which prices are currently too high overall.

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[91] The exact definition may differ on a case by case basis but could be, for example, customers whose tenure with their current supplier is within their initial fixed contract period or who have been with the same provider for less than a certain duration.
[92] Subject to any switching costs.
[93] This is illustrated by the FCA's estimate of the potential waterbed effect of the Basic Savings Rate (BSR) policy option, in the form of lower interest rates to new customers and 'mid-book' customers. See FCA, *Price discrimination in the cash savings market,* July 2018.
[94] See chapter 2.

Table 4.1: Summary of estimates of the loyalty penalty

Market	Number of people/ households (proportion of customers) potentially affected	Total loyalty penalty (per year)	Average penalty per 'loyal' person/ household (per year)	Definition of the penalty	Source
Mobile (handset inclusive)†	1.5 million (6%)	**£330 million**	£222	Overpayment based on estimated average monthly handset charge when acquired with a pay monthly mobile service and number of pay monthly mobile handset contract customers who said they continued to pay the same price outside of their contract period.	Ofcom, 2018.
	4 million (34%)	£473 million	£264	Difference between the initial fixed term contract price and continuing price for people who remain on the contract longer than the initial fixed term length.	Citizens Advice, 2018.
Broadband packages	8.7 million (37% of dual-play and 41% of triple-play customers)	**£990 million**	£112 (£72 for dual-play and £156 for triple-play)	Difference between average spend per customer for 'in contract' and 'out of contract' customers and number of customers 'out of contract'.	CMA calculations
	11 million (43%)	£1,1280 million	£113	Difference between price paid after and during the initial contract period (based on cheapest basic broadband contract) for households which began their current broadband contract at least three years ago.	Citizens Advice, 2018.
Savings accounts	Not known	**£1,136 million**	£48 (typical customer for cash ISA only)	Difference in the average interest rate offered to accounts less than two years old and more than five years old, for people with saving accounts that are more than five years old.	Citizens Advice, 2018 based on FCA, 2018.
Home insurance	12.4 million (47%)	**£709 million**	£13-90, depending on tenure (£57 on average)	Difference between policy price after renewal and the policy price offered to new customers, for people who renew with their provider (ie everyone who has been with the provider with more than a year).	Citizens Advice, 2018 based on FCA, 2015.
Mortgages	0.8 million (10%)	**£800 million**	£1,000	Potential savings consumers who remained on the reversion rate for six months or more could make if they switched to a new two-year fixed deal with the same provider, taking into account that some consumers actively choose to stay on the reversion rate.	FCA, 2018.
	1.2 million (10%)	£527 million	£439	Difference between standard variable rate and fixed rate (also considering fees associated with switching) for people on standard variable rates.	Citizens Advice, 2018.

† We note that the bases for the two data sources are different. For more detail on sources and notes see Annex E.

4.9 Table 4.1 shows that estimates from different sources can arrive at materially different numbers (for example in mobile), which highlights the importance of using robust methodologies when measuring the loyalty penalty. We go on to examine each of the five market estimates in more detail.

Mobile

4.10 For handset inclusive mobile deals, the estimates from Citizens Advice and Ofcom of the number of people affected are very different (4 million and 1.5 million respectively). Both estimates are based on extrapolation of survey data, but these surveys used different methodologies (online survey vs face-to-face), sampling techniques and questioning. This highlights the potential limitations of using survey evidence for estimating the number of affected people and the sensitivity of the results to survey design.

4.11 We note that the estimate from Citizens Advice appears implausible when considered alongside recent Ofcom analysis based on provider data. This Ofcom analysis suggests that the total number of customers who have exceeded their initial contract period and who have mobile with handset contracts is approximately 3.7 million (many of whom will no longer pay charges related to their handset after their initial contract term).[95,96] The estimate by Citizens Advice of customers who are beyond their initial contract term and continue to pay for their handset (4 million) exceeds Ofcom's data on the total number of people beyond the initial contract term.[97] This reiterates the need for more consistent estimates in this market and suggests that Citizens Advice may have overestimated the number of people who pay a loyalty penalty.

4.12 In terms of the average price differential for those who pay a loyalty penalty in mobile, the two estimates presented in Table 4.1 are similar (£264 and £220) but are based on different methodologies.[98] However, while indicative, neither of these methods identify the price actually paid by customers who are beyond their initial contract term or identify a comparator price which takes into account the actual specification of the services purchased by these customers.

4.13 Alternative Ofcom analysis based on provider data finds that, on average, prices beyond the initial contract term are lower than prices within the initial contract term. According to Ofcom, one explanation for this is that some of these customers are not on contracts that require them to continue paying for their handset. Another reason for higher spend within the initial contract term could be a compositional effect, that is, consumers with more recent contracts could have taken out offers with larger data packages and/or more expensive handsets. Uncertainty of the size of the price differential and lack of clarity on what proportion of contracts are likely to result in the customer still paying for the handset after the initial contract period, highlights the need for more work

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95 Some mobile providers offer 'split' contracts whereby the usage and handset element are separated, and the handset element of the change is removed after the expiry of the initial contract period. According to Citizens Advice, providers with around 50% market share offer these kinds of contracts (see page 51 of Citizens Advice, 2018). However, this does not mean that all customers of these providers would be on 'split' contracts.
96 Ofcom, *Consultation on end-of-contract and out-of-contract notifications*, July 2018, page 32.
97 We note that for its calculations, Ofcom gathered data from only a subset of providers and extrapolated the results to the market based on providers' market shares (see Ofcom, *Helping consumers to engage in communications markets*, April 2018, Annex 7).
98 Citizens Advice uses desk research to identify the difference between the price of a selection of mobile handset inclusive deals and equivalent airtime SIM-only deals as the basis for generating an estimate of the difference in prices paid by longstanding and new customers. Ofcom uses provider data to estimate the average cost of a mobile handset provided in a mobile handset inclusive contract as their estimate of this difference.

in this market to understand the severity of the loyalty penalty issue, which Ofcom is currently undertaking

Broadband

4.14 In broadband, Citizens Advice has estimated the loyalty penalty as the difference between listed prices for customers beyond and within their initial contract term. We have estimated the loyalty penalty using data published by Ofcom on the spend by customers beyond and within their initial contract term. The two approaches (review of contracts by Citizens Advice and CMA analysis based on provider data from Ofcom) give similar estimates for the average price difference across products (£113 and £112 per year respectively).[99] However, they arrive at these estimates using very different methodologies. We note that results from other analyses of price differences for broadband packages are broadly consistent, as discussed in Annex E.

4.15 These estimates indicate a significant difference between the prices paid by longstanding and new customers, although they have some weaknesses. As Ofcom highlights, its method does not consider differences in the composition of service purchased by customers. This issue is likely to be particularly important in relation to triple-play packages.[100]

4.16 As a result, the average spend difference could be, at least in part, the result of differences in the types of services purchased by customers within and beyond the initial contract term.[101] Equally, the desk analysis by Citizens Advice does not allow for identifying actual prices paid by consumers or identify comparator prices on a like-for-like basis.[102]

4.17 Ofcom told us that further work was necessary to produce a reliable estimate of the loyalty penalty in broadband. Ofcom said that the triple-play price differential in particular may be affected by differences in the products chosen by in and out of contract customers respectively or reflect differences in the pricing of pay TV. It also said that the figures based on dual-play were more

[99] Our calculation of the penalty based on Ofcom data does not consider the length of period for which the customer pays the higher price. For example, if customers only pay the higher price for a few months, then the numbers presented overestimate the loyalty penalty.
[100] This means that the price difference could be materially different after controlling for service quality differences.
[101] In addition, Ofcom's average spend data does not account for any connection or activation fees charged to new customers, which would increase the average spend of customers within their initial contract term and thus reduce the estimated loyalty penalty.
[102] The actual price paid by customers will often be different from the advertised current price (for example because of negotiations with the provider) and the broadband services purchased may be differentiated by speed, download limitations etc which means that care should be taken to make a like-for-like comparison.

likely to give a reliable indication of the size of the loyalty penalty and would indicate a loyalty penalty in the region of £675 million.

4.18 Therefore, further work is required to identify more robust price differentials, based on data from providers. We understand Ofcom is undertaking this work in its review of price differentials and consumer vulnerability in the fixed broadband market.[103]

4.19 As regards the number of customers who are beyond their initial fixed contract term, there is some difference between the estimates by Ofcom and Citizens Advice. Citizens Advice's survey based estimate suggests that 11.7 million broadband customers are beyond the initial contract term, whereas Ofcom's estimate based on provider data suggests 8.7 million.[104] We consider that provider data is likely to be more accurate and hence the most reasonable available estimate of the loyalty penalty appears to be £990 million, combining Ofcom's published data on the number of people affected and the average price difference.

4.20 This is the best available estimate, although this number should be interpreted with caution because of the limitations of the pricing data. Also, because not all customers who are beyond the initial contract term may pay a penalty (for example because they may have negotiated a better deal with their provider) (see paragraph 4.17). As noted, Ofcom is undertaking further work in this area.

Cash savings

4.21 For cash savings, Citizens Advice's calculations, which rely on provider data collected by the FCA,[105] appear to be the most comprehensive estimate that is currently available on the loyalty penalty. This estimate indicates that the loyalty penalty is a significant issue in this market (£1,136 million per year), measured by the difference in average interest rates of customers who have held accounts for less than two years and those who have held accounts for more than five years.[106] However, it should be noted that the estimate for

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[103] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018. We note that Ofcom's review examines the extent of price differentials by contract status in the fixed broadband dual-play market, but triple-play and quad-play bundles are outside the scope of the review.
[104] The Ofcom number only looks at dual-play (landline and broadband) and triple-play (landline, broadband and TV) whereas the Citizens Advice definition may also capture quad-play (landline, broadband, TV and mobile) customers.
[105] FCA, *Price discrimination in the cash savings market,* July 2018. The analysis is based on a data request from 21 providers on the average balances and interest rates for easy access saving accounts and easy access cash ISAs.
[106] The analysis does not estimate the price difference for those customers who have held an account for two to five years and it does not consider all potential differences in the types of account held by customers of differing tenures.

cash savings is based on relatively old information (from 2013) and therefore may not represent the current situation.

Home insurance

4.22 Producing robust estimates of price differences in home insurance is particularly challenging as there are significant differences across customers in the products purchased, based on their requirements and risk profile. Therefore, average prices across broad customer groups may not give an accurate picture.

4.23 The only available estimate of the loyalty penalty in this market is by Citizens Advice. This combines findings from its consumer research on the proportion of customers who have been with their provider for a specified period of time, with data on price differences from past work by the FCA. However, this estimate should be viewed with caution as each element of the analysis has some limitations.[107]

4.24 As part of its diagnostic work preceding its market study of the general insurance market, the FCA undertook some analysis of how provider margins for home insurance products differ by customer tenure.[108] The work draws on a fairly substantial evidence base and also makes attempts to control for differences in product types.[109] These initial findings support the view that a substantial number of customers stay with their insurance provider for many years, and that the average margin providers earn from individual customers increases substantially with the customer's tenure. The FCA is undertaking further analysis of this issue in home insurance, as well as in other insurance markets as part of its market study.

Mortgages

4.25 For mortgages, both Citizens Advice and the FCA have published estimates of the difference between payments by customers whose introductory deal has ended and are now on a reversion rate, such as a standard variable rate (SVR), and the payments they might make if they were to switch to another deal with the same provider. The two available estimates arrive at different

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[107] The number of people affected is based on consumer research which may be subject to recall bias; the information on price increases over the lifetime of the contract is based on historic information from a limited number of providers; and the pricing information is based on the average cheapest premium which may not be the price paid by the majority of policy holders. In addition, these different pieces of information cover different time periods.
[108] FCA*, General insurance pricing practices: terms of reference,* October 2018, pp 7-8. This analysis shows that 31% of consumers having renewed with their insurer more than five times.
[109] The FCA's analysis is based on a data request to 18 providers that accounted for 40% of policies sold in 2016.

results for both the average difference in payments and for the number of people affected.

4.26 Citizens Advice estimates that 1.2 million people pay £439 on average per year as a loyalty penalty. These estimates are based on desk research (for calculating the rate difference between different mortgage deals) and Bank of England survey data (for the number of people on a reversion rate).

4.27 In contrast, the estimate by the FCA suggests that fewer people pay a significantly higher penalty on average (that is, 0.8 million people pay on average nearly £1,000 per year). This is based on regulatory reporting and transaction data and includes a robust analysis of the number of customers who are paying the loyalty penalty, based on the identification of comparator products for each customer. The FCA also made a number of adjustments to assess whether those on a reversion rate would genuinely benefit from switching:

(a) it excluded customers on a mortgage reversion rate who were coming to the end of their mortgage term or only had a small amount to repay;[110] and

(b) it then assigned a comparator product to the remaining customers based on the most popular two-year fixed rate deal with the same provider for which the customers were eligible. On this basis, about half the customers who were on a reversion rate would have benefitted from moving to the comparator deal.[111]

4.28 Using this approach, the FCA estimated that consumers could have saved approximately £800 million per year in aggregate by switching to a better mortgage deal. We consider this to be the best available estimate of the loyalty penalty in this market.[112]

Limitations in the evidence base

4.29 Existing estimates give a broad indication of the size of the loyalty penalty, but they typically have some limitations, even in cases where numbers from various sources are broadly consistent. These factors may lead to over or

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[110] These exclusions reflect the fact that, after weighing up the benefits of staying on the reversion rate or switching, many customers on reversion rates may choose to stay on them, even if they may be more expensive than alternative mortgage deals.
[111] The other half would not have benefitted from switching because the annual percentage rate (APR) of the new deal (taking account of fees for a new deal) was higher than the APR on the existing reversion rate. This reflects that some customers are on a relatively low legacy reversion rate or that savings from switching to a new deal do not outweigh the costs.
[112] We note that this estimate is based on data from 2016 and more up to date information may give slightly different results.

underestimating the size and the number of people affected. We summarise them here:

(a) most estimates use a broad definition of longstanding customers (for example based on tenure) and do not analyse detailed pricing data to identify those customers who are paying a higher price compared to what they could pay;[113,114]

(b) in many existing estimates, average prices for longstanding customers and average prices of new customers are not compared on a like-for-like basis;[115]

(c) using averages also conceals that some individuals or particular groups of consumers (for example vulnerable consumers) may pay significantly more (or pay the penalty longer) than others. This is further discussed in the following section;

(d) some estimates calculate the loyalty penalty by selecting a given product specification (for example cheapest basic broadband contract) and apply the price difference calculated for this product to all longstanding customers;[116] and

(e) in many cases, the calculations of the total loyalty penalty combine information on the average price differential with data from different sources on the number of affected people, and these components sometimes cover different time periods. This can lead to inconsistencies.

4.30 In order to address these caveats and produce more robust estimates of the total size of the loyalty penalty, regulators and providers should collect and analyse data in a more granular and systematic way, taking into account product differences where possible. In Annex E we summarise the main factors that need to be considered when estimating the loyalty penalty. We set out our recommendations for regulators on the collection, analysis and publication of data on the size of the loyalty penalty in paragraphs 4.54 and 4.55.

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113 In contrast with most other estimates, the FCA's approach to identifying those paying a loyalty penalty in mortgages aimed to do this.
114 Therefore, these estimates may capture people who do not pay more than new customers, for example because they are on good legacy deals or because they negotiated with their provider when the initial contract term came to an end. This can lead to an overestimation of the number of people who pay a loyalty penalty.
115 This is particularly an issue in markets where there is a variety of offers that change over time (for example broadband packages or mobile services) or where the offer is relatively bespoke (for example insurance). This can lead to either an underestimation or overestimation of the loyalty penalty paid by longstanding customers.
116 An exception to this is the FCA's estimate for mortgages which is based on a granular comparison that identifies a benchmark for individual consumers.

Conclusion on size of the loyalty penalty

4.31 Based on the best available estimates, the loyalty penalty across the five markets highlighted by Citizens Advice appears to be around £4 billion in total. The number of people who pay a loyalty penalty varies by market, with estimates ranging from under one million in mortgages to over 12 million in home insurance.

4.32 These estimates give a broad indication of the size of the loyalty penalty in the markets we have looked at, although some of these estimates are more robust than others, and most of them have some limitations. The criteria we have set out for estimating the loyalty penalty (see Annex E) and our recommendations for regulators in paragraphs 4.54 and 4.55 are aimed at improving the existing evidence base by producing robust and informative metrics on the loyalty penalty.

Who is more likely to pay the loyalty penalty?

4.33 Given the additional challenges that vulnerable consumers can face when shopping around and switching, as discussed in chapter 3, we consider here whether they are more likely to be longstanding customers, and therefore more likely to pay a loyalty penalty in markets where it arises. To inform our assessment, we draw on the existing evidence base.

4.34 In doing so, we recognise that some consumers, including vulnerable consumers, may stay with their existing supplier for a range of different reasons. Some consumers may be unable to switch; others may actively choose to stay with an existing provider. This latter group may include some vulnerable consumers, and we found this to be the case for some participants in our qualitative research.

> I don't feel like I need to switch. I'm happy with who I am with and I don't pay a lot so it's not a massive expense.
> Qualitative research participant, physical disability, aged 25-34, Watford.

Mobile and broadband

4.35 The existing evidence base for mobile and broadband suggests that some particular groups of vulnerable consumers - those on low incomes, and the elderly - are significantly more likely to be longstanding customers:

(a) in mobile, Ofcom’s 2018 Switching Tracker showed that those aged 65+ were likely to have been with the same mobile service provider for longer

(43% aged 65+ had been with their provider for 10 or more years, compared with 21% of under 65s);[117]

(b) in broadband, Ofcom's 2018 Switching Tracker found that broadband customers aged 65+ were significantly less likely than those aged 16 to 64 to have ever changed broadband provider (55% vs 67% respectively). Older consumers were also significantly less likely to have changed their broadband provider within the last 12 months (6% aged 65+ vs 12% aged under 65);[118,119]

(c) the 2018 Money Advice Service Financial Capability Survey found that in telecoms (phone, internet and pay TV) markets, consumers on a low income (defined as earning less than £17,500) were significantly more likely to say that they did not shop around for better deals. Around half (51%) of consumers on low incomes, compared to 39% on medium incomes (£17,500 - £49,999) and 31% on high incomes (£50,000+), said they shopped around 'not very much or not at all';

(d) a similar pattern is found for older consumers. Three quarters (74%) of consumers aged 75+ said that they shop around 'not very much or not at all'. Notably, the proportion of respondents saying they did not shop around, increased from the age of 25;[120] and

(e) research by Citizens Advice similarly indicates that in mobile, consumers aged 65+ are likely to stay with their provider after the end of the minimum contract period ended, for longer than people aged under 65.[121] In broadband, consumers aged 65+ and on low incomes, are more likely to stay with their provider for longer.[122,123]

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117 Those aged 65+ were also less likely than under 65s to have ever changed their mobile service provider (50% vs 68% respectively).

118 Ofcom, *Core switching tracker 2018*, 30 August to 30 September 2018. Question 28 'Have you or your household ever changed the company that provides your fixed broadband service? IF YES – When did you most recently change provider for your fixed broadband service? Answer options: In the last 6 months 7 – 12 months ago, 13 – 18 months ago, 1.5 – 2 years ago; 2 – 3 years ago; More than 3 years ago; Have never changed. Tested at 95% confidence level.

119 Consumers aged 65+ are also significantly less likely than average to have considered deals from other broadband providers (17% vs 28% respectively). Source: Ofcom, *Core switching tracker 2018*, 30 August to 30 September 2018. Question 23 and question 27. Activities asked about were: discussed deals/offers with another provider, looked at deals/offers from another provider and talked with friends and family for recommendations about providers.

120 Money Advice Service, *2018 Financial Capability Survey*, (forthcoming).

121 Citizens Advice, *Three of the largest mobile phone providers are overcharging loyal customers*, October 2017 and *Mobile phone networks overcharging loyal customers by up to £38 a month*, October 2017, Citizens Advice, *Reviewing bundled handsets*, September 2018.

122 Citizens Advice, *Exploring the loyalty penalty in the broadband market*, April 2017, Citizens Advice, *Excessive prices for disengaged consumers: a super-complaint to the Competition and Markets Authority*, 2018, page 20.

123 A broadband provider submitted to us that there are no meaningful differences in terms of the likelihood of being out of contract, between different groups of their consumers based on characteristics such as age and income.

Cash savings, home insurance and mortgages

4.36 A similar pattern is found in the three financial services markets: those on low incomes and the elderly are significantly more likely to be longstanding customers.[124] There is also some evidence to suggest that consumers with a physical disability or mental health problems are more likely to have long tenures:

(a) in the three financial services markets, the FCA Financial Lives Survey shows that people with certain characteristics of potential vulnerability[125] are more likely to have long tenures than those who do not show these characteristics. For example, the FCA found that:

i. two-fifths (43%) of those aged 65+ with home insurance (contents and building) have held their insurance with the same provider for 10 years or more, compared with 16% of all adults with this form of insurance. In cash savings, the same proportion of consumers aged 65+ (43%) with a savings account had held it with the same provider for 10 years or more, compared to 27% of all adults with a saving account. In mortgages the proportions were highest, at 72% of consumers aged 65+ and 31% of all adults with a residential mortgage, respectively;[126]

ii. the same survey draws similar conclusions for people with a physical or mental health condition lasting or expected to last 12 months or more. For example, 37% of those with a physical or mental health condition stayed with the same home insurance provider for 10 years or more, compared with 12% who did not have such a condition. A similar proportion (34%) of those with a physical or mental health condition had their savings account with the same provider for 10 years or more, compared with 25% who do not have such a condition. In mortgages the proportions were 48% and 29% respectively;[127] and

(b) in insurance (home and motor), the 2018 Money Advice Service Financial Capability Survey found that 44% of consumers on a low income (defined as earning less than £17,500) said that they shopped around 'not very

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[124] We note that there are other groups of consumers who may also be on a low income but fall outside of the definitions here, which other research has found to benefit from shopping around and switching. For example, the FCA found that unemployed renters and those with low credit scores had a tendency to shop around in home insurance. Source: FCA, *Pricing practices in the retail general insurance sector: household insurance*, 31 October 2018.
[125] The definition takes into account a wide range of characteristic, including: low financial resilience, experience of recent life events, low financial capability, health issues.
[126] FCA, *The financial lives of consumers across the UK: key findings from the FCA's Financial Lives Survey 2017*, 20 June 2018.
[127] FCA, *The financial lives of consumers across the UK: key findings from the FCA's Financial Lives Survey 2017*, 20 June 2018.

much or not at all', compared to 23% on medium incomes (£17,500 - £49,999) and 15% of consumers on high incomes (£50,000+). Over half (56%) of those aged 75+ said that they had shopped around 'not very much or not at all' in insurance, a significantly higher proportion than for any other age group. The proportion saying that they did not shop around, increased from the age of 25.[128] Both Citizens Advice and Which? have found that consumers aged 65+ or 75+ are more likely to have longstanding policies in home insurance when compared to the rest of the population.[129]

4.37 In summary, the available evidence indicates that older consumers and consumers on low incomes are more likely to stay longer with their providers in the five markets. In financial services, survey results also show that people with other vulnerabilities, such as a physical or mental health condition, are more likely to have long tenures. As a result of being longstanding customers, these groups of vulnerable consumers may be more likely to pay a loyalty penalty in these markets.

Limitations in the evidence base

4.38 There are gaps in knowledge about different groups of vulnerable consumers due to a lack of research and data.

4.39 In mobile and broadband, while there is data and evidence on age and some focus on income in existing research, there are some gaps in the profile of vulnerable people paying the loyalty penalty. We note that Ofcom has recently launched a review of price differentiation in the fixed broadband market which will have a particular focus on vulnerable consumers, which may include people who are older, on low incomes, or who have a physical disability or mental health problem.[130]

4.40 In the financial services markets, while the FCA collects data on vulnerable consumers through its Financial Lives Survey, there are gaps - for example specific data on mental health conditions is not collected at present.[131]

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[128] Money Advice Service, *2018 Financial Capability Survey* (forthcoming).
[129] Citizens Advice, *The insurance loyalty penalty: unfair pricing in the home insurance market*, November 2017, Citizens Advice, *Excessive prices for disengaged consumers: a super-complaint to the Competition and Markets Authority*, 2018, page 20, Which?, *Loyal customers pay 38% more for staying with their home insurer*, 28 August 2018.
[130] As part of its review of price differentiation in the fixed broadband market, Ofcom has undertaken preliminary analysis on the data that providers hold on vulnerable consumers. This has highlighted inconsistencies in data collection practices, for example different providers recording different categorisations of vulnerability. Ofcom will be considering this as part of its review. Further details are available on Ofcom's website, see also Annex C.
[131] We note that a general wellbeing question which includes 'mental health' as a response category is included in the FCA Financial Lives Survey.

4.41 Therefore, while there is an evidence base for some groups of vulnerable consumers - such as older consumers - the data for other groups is limited.

4.42 In addition, existing studies focus only on whether particular groups of vulnerable consumers have been with the same provider for a long time, or whether they are in or out of contract. While this provides a high level indication of the likelihood of these groups paying a loyalty penalty,[132] it does not directly measure whether they are in fact paying a loyalty penalty, the size of any loyalty penalty and whether vulnerable consumers on average pay a higher penalty than others across key markets. This sort of evidence can only be produced by matching price data from suppliers to survey data, which is why we recommend to regulators that they assess the feasibility of undertaking such a data matching exercise, as set out in paragraphs 4.54 and 4.55.

Conclusion on who is more likely to pay the loyalty penalty

4.43 Vulnerable consumers are more likely to be longstanding customers and stay with their provider out of contract, on auto-renewed or roll over contracts. This indicates that vulnerable consumers may be more likely to pay a loyalty penalty where it arises.

4.44 However, the existing evidence base does not allow for further conclusions to be drawn; it is currently not possible to establish whether vulnerable consumers are indeed paying a loyalty penalty, and whether they on average pay a higher penalty than others. Therefore, further work is needed to address these evidence gaps.

4.45 We set out a recommendation for filling this evidence gap in the next section. In subsequent chapters and throughout this response, we consider whether additional protections should be put in place for vulnerable consumers and what these might look like, to help tackle the loyalty penalty for these groups.

Filling gaps in the evidence base

4.46 We noted in the previous two sections that there are some gaps in the evidence base that hinder our ability to understand the size of the loyalty penalty in different markets, and who pays it.

4.47 Currently, regulators can address these questions through market studies that allow price data from suppliers to be linked to consumer surveys that include

[132] While the length of the contract/relationship with the same provider can be indicative, this does not consider the fact that consumers may stay with the same provider but negotiate a better deal.

demographic characteristics. These give powerful insights but are conducted on an ad hoc basis, with evidence becoming out of date over time. Furthermore, such studies do not allow for comparisons across markets.

4.48 We have therefore considered the scope for identifying whether the loyalty penalty is paid by different subsets of consumer on an ongoing basis, and across markets. A potential way of doing this would be to 'match' price and tariff data (such as on tariff type, and tenure) from the five markets with a recurring survey that contains comprehensive information about respondents' characteristics, including those associated with vulnerability (age, income, etc). This data would be provided by suppliers in the markets, which regulators would collect using their data gathering powers.

4.49 Such an approach would potentially provide a number of significant benefits. In particular, linking transaction data from several markets to a high quality recurring survey would allow us to compare outcomes across markets, to identify whether the same individuals are suffering from poor outcomes in different markets. Matching transaction data to a longitudinal survey would have the further advantage of offering opportunities for understanding the experiences of consumers over time and providing a baseline against which regulators can consider how and why particular problems are occurring, and for whom. As one party's submission to our invitation to comment stated, 'an aligned approach would enhance regulatory efforts to protect vulnerable consumers'.

4.50 We recognise that a number of practical implementation issues would need to be addressed in assessing the suitability of this approach, including for example, identifying the types of price data that could be collected and a suitable recurring survey to which they could be matched. We are therefore recommending that the regulators undertake a feasibility study into the scope for such data matching; this could be taken forward through the UK Regulators Network (UKRN).

Regular publication of estimates of the loyalty penalty

4.51 Robust estimates of the loyalty penalty in different markets are of clear value to regulators. It would help them to decide which markets they should investigate further and enable them to evaluate the impact of their interventions on the size of the loyalty penalty over time or for particular groups of consumers. In addition, we believe there is a strong case for regularly publishing estimates of the loyalty penalty. This can incentivise companies applying the loyalty penalty to change their behaviour, inform public debate and raise general awareness.

4.52 Reputational incentives can be a powerful force in recognising and rewarding good conduct and discouraging exploitative behaviour or unsatisfactory performance. The potential impact on businesses' brand value of reputational harm can focus minds at board level. Publishing business-level estimates of the loyalty penalty, and the associated media coverage and customer awareness, may prompt suppliers to offer better deals to longstanding customers and reduce the price differential in order to build a good reputation.[133]

4.53 We therefore recommend that regulators should collect and publish indicative metrics on the existence and size of the loyalty penalty (ie price differences or number of longstanding customers) on a regular basis (such as annually, through for example a loyalty penalty report).[134] Alongside this, other potentially relevant metrics could be published such as switching levels, call waiting times and potentially speed of exit and entry (see chapter 7 for a discussion of these issues).This could be taken forward through the UKRN's work on performance scorecards, as set out in the government's consumer green paper.[135]

Recommendations

4.54 Producing and publishing estimates of the loyalty penalty in key markets can help regulators to design, prioritise, target and evaluate interventions. Publishing information on price differences may influence the pricing of providers.

4.55 Taking this into account, we have made two recommendations in relation to key markets where the loyalty penalty arises. In doing so, we recognise that there is ongoing relevant work by regulators and others, such as the UKRN, in some of these areas. We expect these recommendations to complement and build on this existing work as appropriate, or to be started where it has not yet been carried out:

(a) Regulators should explore the feasibility of producing and publishing robust estimates of the size of the loyalty penalty and who pays it, taking into account the principles set out above, for example through the UKRN.

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133 Examples of this kind of reputational incentive include Ofgem's SVT league table and SVT quarterly indicator. As Ofgem told us, the information from these publications have been promptly and prominently captured by the media. This can act as a powerful prompt for customers which is demonstrated by the fact that some of the biggest energy switching peaks observed to date have coincided with high levels of media attention on the large energy suppliers. This, in turn, puts pressure on the prices charged by energy suppliers.
134 We note that regulators already publish information on prices: for example, information on pricing trends for communication services is published annually by Ofcom.
135 BEIS, *Modernising consumer markets consumer green paper*, April 2018, paragraphs 68-69.

In particular, regulators should assess the feasibility of collecting data from providers and linking the findings from a recurring consumer survey containing information on consumer characteristics[136] to pricing and tariff information from providers, to identify the size of the penalty (by individual customers and in aggregate) across markets, for example through the UKRN.

(b) In line with the government's consumer green paper,[137] regulators should capture and publish informative and simple metrics on the loyalty penalty on a regular basis. These could, for example, be published in an annual loyalty penalty report, in the context of the specific sectors where it arises, including information related to individual suppliers.

[136] To the extent data on consumer characteristics is gathered by providers, regulators should also aim to capture this data.
[137] BEIS, *Modernising consumer markets: consumer green paper*, April 2018, paragraphs 68-69.

5. Approaches to tackling the loyalty penalty

- Regulators can act in various ways to tackle the loyalty penalty. Interventions range from 'lighter touch' information and disclosure remedies as well as other more active measures to help consumers to find better deals, taking enforcement action against specific supplier practices and regulating prices directly.
- Performance-based regulation and reputational incentives can help encourage suppliers to act in the best interests of consumers.
- Publishing business-level estimates of the loyalty penalty in key markets and for each supplier, would be beneficial in putting pressure on suppliers to act to reduce it, while also raising awareness of the issue.
- To maximise the impact of remedies, regulators should consider explicitly the needs of vulnerable consumers to ensure they are able to benefit from planned interventions.
- Regulators should work together to learn from past experience, capturing best practice on remedies introduced to promote consumer engagement and their effects.

Introduction

5.1 This chapter summarises the types of action that could be taken (ie remedies) to address the causes of the loyalty penalty and its impact on consumers. Subsequent chapters consider these remedies in further detail, as well as their application to the five markets: mobile, broadband, cash savings, home insurance and mortgages.

5.2 This chapter is structured as follows:

(a) a description of what we are trying to achieve with remedies;

(b) an overview of the different remedy strategies that are available to address the loyalty penalty;

(c) an outline of the main factors that are relevant to choosing between remedy options;

(d) key points on maximising the impact of remedies; and

(e) recommendations on the different remedy approaches.

What we are trying to achieve with remedies

5.3 The goal of interventions to tackle the loyalty penalty should be to ensure that existing customers are able to get a fair deal for goods and services without having to exercise unreasonable effort, taking into account their expertise, circumstances and capabilities.

5.4 In pursuing this goal, regulators generally should avoid measures whose negative consequences outweigh the benefits they generate. An example would be remedies that narrow the loyalty penalty, but which result in very large costs or inefficiencies that leave all customers worse off (ie higher overall prices). As discussed in chapter 2, where there are concerns around fairness, it may be desirable for regulators to put in place targeted interventions to protect certain consumers.

Different remedy strategies to address the loyalty penalty

5.5 Our response considers three main ways in which regulators can act to improve outcomes for existing customers who are paying a loyalty penalty.[138] This reflects the variety of causes of the loyalty penalty and its severity in different markets. These three broad strategies are:

(a) helping consumers engage and switch to better deals;

(b) stopping harmful business practices; and

(c) regulating prices.

Helping consumers engage and switch to better deals

5.6 A major focus of regulators to date has been on interventions aimed at helping consumers engage with the market and switch to better deals.

5.7 Building on earlier work and research,[139] we know that to motivate engagement and switching, consumers need accurate information, sufficient time, reward and opportunity to assess products or service offerings and the option of acting by switching to a new provider or product.

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[138] In assessing the super-complaint, the CMA has not made any findings nor formed an opinion about the possible effects on competition of practices or regulating provisions of the FCA or features of the market that could be addressed through practices or provisions of the FCA. It follows that none of the recommendations in this response can amount to advice to the FCA under section 140B of FSMA.
[139] UKCN, *Helping people get a better deal: lessons learned about consumer facing remedies*, October 2018. See also Professor Amelia Fletcher, *Disclosure and other tools for enhancing consumer engagement and competition*, 2018.

5.8 However, people often do not operate as ‘ideal’ or ‘textbook’ consumers. As detailed in chapter 3, individuals’ income, physical and mental health, age, demands on their time and other aspects of vulnerability, may restrict their ability to access, assess and act to get better deals. For this reason, remedies which actively help consumers, for example to interact in markets, shop around and/or make the process of switching easier, are more likely to be effective in tackling the loyalty penalty than those which, for example, simply provide information.

5.9 Remedies aimed at improving consumer engagement and switching are covered in more detail in chapter 6.

Stopping harmful business practices

5.10 Suppliers can also make it more difficult for existing consumers to get better deals, as it is often profitable for them to do so. For example, they may present information about price changes in a way that fails to make clear that a price rise has occurred. They can also make the process of switching more difficult for existing consumers, for example, requiring customers to cancel their contract in writing, or by telephone and being kept waiting, in order to exit a contract.

5.11 It is therefore also necessary to tackle the behaviour of suppliers so that they are not complicating, obstructing or confusing consumers and their decision making.

5.12 Each of these issues, along with possible remedies, are considered in detail in chapter 7.

Regulating prices

5.13 Remedies can also be designed to regulate prices directly in order to limit the harm arising from the loyalty penalty. Regulators should consider targeted pricing regulation where engagement remedies and measures to tackle harmful business practices are unlikely to be sufficiently effective in driving competition, would only act slowly, or would not adequately protect the interests of some consumers, particularly the vulnerable. These types of remedies directly address the harm arising from the loyalty penalty as they restrict prices, for example, by limiting price differences or introducing absolute price caps. They can be targeted at particular groups of consumers in markets, such as those most affected by the loyalty penalty particularly if they are vulnerable.

5.14 Pricing remedies and how they can be targeted, are discussed in detail in chapter 8.

Choosing between remedy options

5.15 As set out earlier, a variety of different approaches are available to regulators to tackle the loyalty penalty. Some approaches, for example enforcing basic standards of transparency and taking action against harmful business practices, are likely to be of wide application. Others will need to be considered on a case by case basis. For markets with deep-seated problems, a range of interventions may be needed.

5.16 The choice between remedy options to tackle the loyalty penalty in any given situation will depend on a range of factors, including:

(a) the underlying causes and size of the problem (see chapter 2);

(b) the extent to which the problems identified in a market are entrenched; and

(c) the characteristics of consumers who are adversely affected, particularly where vulnerable consumers may be experiencing harm (see chapter 3).

5.17 The overarching principles by which regulators are guided include two key considerations:[140]

- effectiveness: the need to choose remedies that will succeed in tackling the loyalty penalty and secure better outcomes for consumers; and
- proportionality: the duty on regulators to act reasonably, not to impose unnecessary burdens and to ensure that remedies do not give rise to unintended consequences that outweigh the benefits.

Maximising the impact of remedies

5.18 We set out some key points that are important in maximising the impact of interventions to secure a better deal for existing customers. Regulators can do this by:

(a) focussing on supplier behaviour;

(b) being clear about the outcomes that remedies seek to achieve;

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[140] CMA, *Guidelines for market investigations*, April 2013.

(c) giving greater consideration to the needs of vulnerable consumers; and

(d) using evidence and experience to guide thinking.

Focussing on supplier behaviour

5.19 We think that there needs to be a rebalancing of regulatory attention, with more emphasis on the behaviour of suppliers.

5.20 Charging less active existing customers a high price for goods or services is a decision that is made by suppliers, not customers. However, much of past debate and many previous interventions have focussed on improving consumer engagement as a means of increasing switching and increasing pressure on suppliers. As we set out in chapter 6, there are useful consumer-focussed interventions that can make a positive difference, and more can be done to make these remedies more effective. However, consumer behaviour is itself significantly influenced by conditions set by suppliers.

5.21 There are a number of ways in which regulators and government can work together to alter suppliers' incentives, so that they no longer perceive it to be in their commercial interest to dampen consumer engagement and exploit their existing customer base, and instead focus on offering a better deal to all consumers:

(a) robust enforcement is essential to ensure that suppliers take their regulatory and consumer law obligations seriously. The ability to impose fines and penalties for non-compliance is a vital tool that is available to some regulators and should be actively used;

(b) reputational incentives can be a powerful force in recognising and rewarding good conduct and discouraging exploitative behaviour or unsatisfactory performance. The potential impact on businesses' brand value of reputational harm can focus minds at board level. Publishing business-level estimates of the loyalty penalty in line with the principles set out in chapter 4, for example, would raise awareness of the issue and put pressure on suppliers to act to reduce it. To be effective, reputational incentives need to be easily understandable, powerfully communicated and based on comparable data. Publication of fines and completed enforcement action against businesses can also have a powerful reputational and deterrent effect; and

(c) positive incentives to innovate and disrupt markets can also be a powerful force for change. Regulators can play a proactive role in facilitating the entry and expansion of businesses that introduce innovative models that improve outcomes for consumers. The creation of prize funds, such as the Nesta Open Up Challenge, is one way of facilitating such entry.[141]

Clarity about the outcomes that remedies are seeking to achieve

5.22 There should also be greater clarity about what remedies are seeking to achieve.

5.23 Some previous interventions (for example compliance disclosures) have focussed on requiring suppliers to take a particular action, with the presumption that having done so, suppliers' regulatory obligations towards consumers had been fully discharged. This can mean suppliers do not take accountability for the ultimate outcomes that consumers experience.

5.24 Performance-based regulation is an innovative approach that seeks to shift attention towards better consumer outcomes, while holding suppliers accountable for delivering those outcomes.[142] It has three key components:

(a) a regulator determines the outcomes for consumers that suppliers need to deliver. For example, a regulator might target improvements in service quality, or consumer understanding of terms and conditions;

(b) the regulator sets up a process for auditing suppliers' performance in delivering these outcomes. This might involve measurement of observable performance indicators – such as how much time it takes to exit a contract – or research with consumers, for example on whether they are aware of a particular contract term that affects them (for example the length of a minimum contract period); and

(c) the regulator establishes a framework of sanctions for underperformance, which aligns the goals of the regulator and the incentives of the supplier. Sanctions might be financial (for example penalties), reputational (for example 'naming and shaming') or commercial (for example contracts may be deemed unenforceable if few consumers understand them).

5.25 Having set this framework, regulators could focus less on precisely how suppliers deliver better outcomes. Instead, it gives suppliers flexibility to determine how to achieve the desired outcomes most efficiently. Suppliers can tailor approaches to different consumer segments (for example vulnerable consumers) and adapt approaches over time. It also avoids the 'game playing'

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[141] Ofgem is currently working with Nesta on a challenge programme aimed at identifying innovative ways of stimulating switching in the energy market, following recommendations made by the CMA in its energy market investigation. See the Open Up Challenge webpages for further details

[142] Lauren E Willis, *Performance-based consumer law*, 82 University of Chicago Law Review,pp 1309, 2015.

that can arise where regulation focuses more narrowly on specific supplier behaviour. This approach has potential for application in relation to the loyalty penalty, particularly regarding the various harmful business practices discussed in chapter 7.

Greater consideration of vulnerable consumers

5.26 Regulators need to continue to pay greater attention to the needs of vulnerable consumers.

5.27 An exclusive emphasis on transparency or smart nudges may leave some people behind. As set out in chapter 3, some groups of vulnerable consumers may be more likely to experience the loyalty penalty as they can face additional challenges to switching and negotiating with suppliers.

5.28 Regulators should explicitly take these challenges into account when designing remedies and consider additional targeted protections, such as pricing interventions, where needed.

Using evidence and experience to guide thinking

5.29 Regulators need to be guided by evidence about the likely success or failure of different approaches in tackling the loyalty penalty.

5.30 The experience of previous demand side interventions has been variable.[143] Over the past five years, regulators have focussed much more on evaluating the likely impact of interventions. This should continue, particularly in the following areas:

(a) testing and trialling potential remedies before implementation where possible. Consumers can behave differently in practice to how regulators anticipate. Testing can be used to compare the efficacy of various remedies, individually and as a package. It also means that remedy design can be amended to achieve maximum impact;[144] and

(b) evaluating whether remedies have had the desired impact after they have been put in place. Regulators should review previous interventions to ensure that they have been properly implemented and are acting as

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[143] Professor Amelia Fletcher, *Disclosure and other tools for enhancing consumer engagement and competition,* 2018.
[144] UKCN, *Helping people get a better deal: lessons learned about consumer facing remedies*, October 2018, chapter 5.

intended. For example, consumers may change their consumption patterns following full scale roll out of an intervention.

5.31 Regulators should work together to share and capture best practice around remedies to promote consumer engagement, including where remedies have failed to have the intended effect as well as where they have been successful in increasing switching rates. Future interventions could be improved by applying lessons learned from other regulators.

Recommendations

5.32 Regulators have grappled with issues relating to the loyalty penalty over many years, but the problem clearly remains material in many markets. While regulators are becoming more effective in designing and testing disclosures and 'nudge' type remedies, many existing and longstanding customers are still getting a bad deal. Too much has been asked of consumers and not enough has been demanded of suppliers.

5.33 Based on our review of past remedies in the five markets and more widely, we think a step-change is needed in terms of how we and regulators tackle this issue. In our view, the most promising approaches are:

(a) actively helping people engage and move to a better deal, through smart data, intermediaries and collective switching (see chapter 6);

(b) enforcement to tackle harmful and exploitative supplier practices (see chapter 7); and

(c) a greater willingness to use targeted price controls where there is substantial harm to some consumers, particularly where this harm impacts those who may be vulnerable (see chapter 8).

5.34 We consider these approaches in detail in the following chapters. Within each, we focus on the need for additional or targeted measures for vulnerable consumers.

5.35 We also recommend that further work is undertaken by regulators to capture and share best practice on 'nudge' remedies, to ensure that lessons are learnt on when these types of remedies are more or less effective. This could be taken forward by the UK Competition Network.

6. Helping people engage and switch

- Regulators have become more adept at developing and testing information remedies which prompt people to search for and switch to better deals ('nudges'). While this encourages some consumers to switch, new and bolder measures are needed to help people find better deals, especially those hardest to reach.
- Emerging technologies can be revolutionary. Putting people in charge of their own data means that consumers can find the best deals for their needs and can empower intermediaries, such as automatic switching services, to act on their behalf.
- In mobile and broadband, the complexity of tariffs makes data-driven technologies particularly powerful.
- Innovative intermediary services can encourage shopping around by greatly reducing the costs of searching and switching. In all five markets, regulators should maximise the opportunities for consumers to benefit from these technologies by creating favourable conditions for their development.
- Collective switching is another potential route to engaging consumers. Ofgem's recent collective switch trial shows what can be achieved. We recommend that Ofcom and the FCA consider its feasibility for broadband and cash savings.
- These remedies have the potential to engage many more people in the five markets, to help protect them from the loyalty penalty.

Introduction

6.1 In this chapter we examine various measures intended to help existing customers engage in markets and switch providers. We consider approaches that have been tried to date in different markets and in which situations these measures are most likely to be effective in tackling the causes of the loyalty penalty. We then assess their current use and likely effectiveness in the five markets covered by the super-complaint. This chapter is structured as follows:

(a) a summary of engagement remedies, covering:

i. information remedies;
ii. smart data;
iii. intermediary-based remedies; and
iv. collective switching;

(b) the applicability of engagement remedies to the five markets; and

(c) recommendations.

Summary of engagement remedies

6.2 The measures that we discuss in this chapter are aimed at promoting consumer awareness and reducing friction in the 'customer journey' from one supplier or product to another. Interventions can be targeted at different stages of the customer journey and can vary in the degree of help that they provide – ranging from information disclosures to actively providing assistance to consumers to compare or switch suppliers.

6.3 In some cases, interventions have been intended to prompt (or 'nudge') consumers to take action themselves. In other cases, regulators have sought to encourage the entry of intermediaries whose role can vary from simply identifying better deals for customers through to actively managing their move to a new supplier.

6.4 Historically, regulators have frequently focussed on the design of information remedies. As set out in chapter 5, the provision of accurate and timely information to consumers continues to play a significant role in making markets work generally. However, there is a need for additional interventions – such as smart data, intermediary-based remedies and collective switching – that can provide active help and support to less active customers. We explore information remedies as well as these newer solutions in this chapter.

Information remedies

6.5 Remedies which increase transparency in markets help consumers to compare products and services and make well informed decisions. In designing information-based ('disclosure') remedies, regulators need to consider carefully how consumers make decisions in practice, being conscious of the demanding lives that people lead and the multiple and varied priorities competing for their attention.

6.6 Disclosure remedies aimed at tackling the loyalty penalty need to be clear and understandable and, ideally, designed in such a way as to increase the relevance of the decision in consumers' minds. Through targeted timing of interventions, for example at important trigger points in a customer's relationship with their supplier (such as towards the end of a minimum contract period), regulators can maximise the likelihood that existing consumers will engage with the information being provided and will be prompted to take action.

6.7 Over recent years, regulators have become more adept at designing information remedies. These increase transparency in markets and act as prompts to remind existing consumers to consider their options and to help them switch to a better deal.

6.8 Experience shows that well-designed and properly tested information remedies can have some success in prompting existing customers to engage and get a better deal. For example, following testing of various types of disclosure, the FCA found that including last year's premium on renewal notices prompted 11 to 18% more customers to switch or negotiate their insurance policy.[145]

6.9 In our view, this type of disclosure is worth testing and, if it increases switching, implementing in other markets. Its effect could be strengthened by requiring providers to prominently display complementary information, such as the cumulative effect of price rises since the customers' initial contract.

6.10 This information could raise awareness of the impact of price walking in some markets (such as insurance). By clearly displaying the consequences of remaining with a single provider for a long period of time, it could also alert consumers to the importance of shopping around and if necessary, switching.

6.11 Ofgem's recent collective switch trial has produced some useful insights into how disclosures can be designed to appeal to less active, longstanding customers who can be difficult to engage (see paragraph 6.57 for further detail). The trial demonstrates some useful examples of good practice in disclosure remedies which may be applicable to other markets, including:

- the provision of personalised projected savings to attract consumers' attention;
- offering multiple information channels and routes to action the switch (for example telephone as well as online) to appeal to different customers' needs;
- having a clear deadline to increase saliency, combat inertia and trigger action; and
- using a trusted messenger (for example a regulator, government) to instil confidence and credibility in the remedy.[146]

6.12 However, despite some success, evidence also suggests that information remedies may not be sufficient in all markets and for all consumers. This is

[145] FCA, *Increasing transparency and engagement at renewal in general insurance markets*, December 2015.
[146] Similar themes emerged from our commissioned qualitative research. See BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018, chapter 7.

because they place the onus of finding and moving to a better deal almost entirely on consumers, which can require considerable attention, effort, perseverance and resourcefulness on their part. Providing information to consumers is often not enough to trigger action, particularly among those who face the most difficulty when participating in markets, such as vulnerable consumers.

The power of smart data

6.13 Since smart data cuts across many of the engagement remedies, we begin with an explanation of the concept, describe its application to the retail banking sector and explore its use in other markets.

6.14 Smart data is a term used to denote data-driven technologies and services to improve consumer outcomes in regulated markets.[147] It can help consumers affected by the loyalty penalty in two ways:

- it can make it easier for people to find good deals by themselves, by helping them understand their usage and the products most suited to their needs; or
- it can help intermediaries do that job, and more, for consumers.

6.15 While we believe that smart data has tremendous potential, we also recognise that technological innovation is unlikely to be a solution to all of the problems associated with the loyalty penalty. We are particularly mindful that some vulnerable and/or inactive consumers, particularly those who are not digitally active, face additional challenges and require additional support or protections.

6.16 Smart data is not a single remedy in itself but provides a platform for enabling other specific interventions in markets which may themselves be led by private sector innovators, government or regulators, or by the third sector.

6.17 The government is currently conducting a Smart Data Review to consider how it can accelerate the development and use of data-driven technologies and services in regulated markets. The review will consider intermediary services such as automatic switching, as well as new business models.[148] It aims to

[147] BEIS and Department for Digital, Culture, Media and Sport, *Smart Data Review: terms of reference*, September 2018.
[148] BEIS, *Modernising consumer markets: consumer green paper,* April 2018, page 23.

build on the work being pioneered in the retail banking sector by Open Banking.[149]

6.18 Open Banking is currently among the most advanced applications of this approach in any market worldwide.[150] Following the CMA's market investigation into retail banking,[151] we required the nine leading banks in the UK to adopt common and open application programming interfaces (APIs),[152] data and security standards. It enables consumers and small businesses to share their banking transaction data securely with trusted third party providers (TPPs) of banking services. These services fall into two main categories:

(a) those whose functionality is described as 'read-only' and which help the consumer manage their personal finances (for example aggregators) or identify the best value products for them (such as PCWs); and

(b) those which take a more active role in managing a consumer's finances, including moving money into and out of their payment accounts - described as 'read/write' functionality.[153]

6.19 Open Banking services in the first category (read-only) facilitate shopping around. For example, a consumer can share their transaction history with a PCW, which can then offer information about other current accounts which might better fit the way they use their account.[154]

6.20 This type of service is, clearly, most useful where providers charge per transaction and where consumer usage patterns are highly differentiated. The use of smart data can help provide personalised projected savings, making comparisons more relevant to consumers. It is therefore likely to be highly relevant in the mobile and broadband markets.

6.21 Services in the second category (read/write) are capable of offering more proactive help to consumers.

6.22 The Smart Data Review is currently exploring applications of the principle of data sharing in the regulated sectors. Its conclusions will be announced in the first half of 2019. Although Open Banking has been 'live' for just over six

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[149] HM Treasury has also established a Digital Competition Expert Panel led by Professor Jason Furman which is examining the UK's competition regime in the context of the digital economy.
[150] The concept is being extended to the energy and telecoms sectors in Australia through the implementation of the Consumer Data Rights legislation.
[151] CMA, *Retail banking market investigation final report,* August 2016.
[152] APIs enable applications to share data and functionality. They are commonly used in consumer applications, for example where one user's location is shared with another.
[153] These broadly correspond to the distinction between account information service providers (AISPs) and payment initiation service providers (PISPs) in the revised Payment Services Directive (PSD2).
[154] For example, by taking account of the number of times and the extent they overdraw, or the number of foreign currency transactions they make a year.

months, it is possible to draw some provisional conclusions on its effectiveness and thus its potential relevance to other markets.

6.23 Based on the experience to date, read-only smart data solutions which provide consumers with better information or tailored recommendations – such as ‘smarter’ PCWs – seem most likely to be effective where usage patterns are highly differentiated and where providers’ pricing models are based on usage.

6.24 Read/write functionality, as described in paragraph 6.18, has a great deal of potential for tackling the loyalty penalty for some consumers. This is because it enables certain intermediaries (which we refer to as ‘concierge’ services) to overcome consumers’ inability or unwillingness to change suppliers or products, by automating this process. Such services have the potential to be of considerable value for less active consumers.

6.25 Consumers are likely to have concerns regarding the security of the data they are sharing and the trustworthiness of the entities with whom they are sharing it. Unless consumers feel secure sharing their data, they will be unlikely to use services facilitated by smart data. Smart data remedies, therefore, need to be accompanied by ancillary measures to build confidence in the security of data shared. For example, in Open Banking, TPPs are regulated by the FCA.[155]

6.26 Overall, we believe that the use of smart data has great potential as part of a wider strategy for tackling the loyalty penalty in a number of markets. It is important, however, that issues regarding consumer trust are considered in the implementation of smart data remedies.

6.27 While this important work takes place, regulators may want to look at other, interim measures to help consumers to benefit from their own usage data. In markets where open, standard APIs have not been adopted by the industry to facilitate data sharing, providers could be required to make relevant usage data easily available to customers in ways that can be used to make comparisons, for example via an app.

Using intermediaries to empower and support consumers

6.28 New technology and smart data are opening up more possibilities to help consumers, but we also recognise the importance of personal support, particularly for vulnerable consumers.

[155] See the FCA website. Additionally, the Open Banking Directory enables banks to verify the identity of TPPs. Further, in terms of redress, under PSD2, consumers are entitled to compensation from their bank if an unauthorised payment is made.

6.29 We next consider the potential role that can be played by different types of intermediaries in supporting and empowering consumers, to help them achieve a better deal and avoid paying a loyalty penalty. The role played by intermediaries varies, including the amount of practical help they offer consumers.

6.30 We consider four broad categories of intermediary:

(a) PCWs;

(b) concierge services (also known as automatic switching services);

(c) switching services; and

(d) human intermediaries.

PCWs

6.31 PCWs are a well-used and understood feature of many retail markets. They are run on a commercial basis often by well-resourced businesses and can come in a variety of forms. Simple PCWs will categorise deals in a variety of ways (for example by price), leaving the consumer to check whether their offerings match their particular requirements.[156] Data sharing has the potential to enhance the usefulness of PCWs by enabling them to provide information tailored to the needs of individual consumers.

6.32 PCWs generally benefit consumers in two main ways:

- they make it easier for people to shop around, saving them time and effort, particularly in markets that can be complicated and uninteresting; and
- they make suppliers compete harder by providing lower prices and better choices to consumers.

6.33 The CMA conducted a market study in 2017 in this area and we noted that PCWs can also benefit people who do not use them.[157] This is because the competitive pressure that they exert on suppliers drives competition more generally.[158]

[156] For example, a PCW may list loan products with their APRs, terms and conditions but will not generally be able to relate the terms that an individual will be offered on the basis of their creditworthiness and the lender's eligibility criteria.
[157] CMA, *Digital comparison tools market study final report,* September 2017.
[158] CMA, *Digital comparison tools market study final report,* September 2017, pp 43-46. In October 2018, the UK Competition Network also published a report on lessons learned about consumer facing remedies which contains principles for supporting the development of PCWs and good practice to ensure they work well for consumers. See UKCN, *Helping people get a better deal: lessons learned about consumer facing remedies*, October 2018, page 30. Similarly, recent work by Professor Amelia Fletcher sets out ways to develop third party comparison

6.34 As part of our market study, we noted the harmful impact that non-resolicitation clauses can have on competition between suppliers, particularly where they cover a customer's renewal period.[159] These clauses limit the ways in which consumers can receive prompts to engage and shop around. Their effect on consumers remains of interest to the CMA.

6.35 Commercially-funded PCWs rely on consumers being willing and able to seek out information and then act on it. This in turn generates commission revenue from the provider acquiring the new customers. PCWs therefore have a business incentive to promote consumer engagement. They have made significant investments in advertising the benefits of shopping around and switching as well as using rewards to encourage ongoing comparisons.[160]

6.36 Where consumer engagement is very low, PCWs may find the market relatively unattractive and be unwilling to invest in it. There have been instances of regulators requiring the funding and creation of PCWs.[161] The CMA, for example, required the major banks to fund a challenge prize, managed by Nesta, to encourage the creation and market entry of DCTs for SMEs.[162]

6.37 PCWs offer a range of different approaches, from static lists of 'best buy' tables to generating tailored quotes based on individual customer requirements and/or usage patterns. As new approaches to data sharing are developed, more sophisticated PCWs are becoming available which can provide bespoke recommendations (for example using a customer's historic patterns of usage). Where PCWs can access supplier information, potentially through an open data licence, or where consumers grant access to usage data from their incumbent supplier, PCWs can provide more useful comparisons more easily. Smart data can therefore facilitate the comparison of complex usage patterns.

6.38 'Smarter' PCWs are likely to provide more useful comparisons in some markets. However, the onus will still be on consumers to act, as PCWs will identify suitable deals and offer information, rather than actively helping people to switch.

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tools and to facilitate their development. See Professor Amelia Fletcher, *Disclosure and other tools for enhancing consumer engagement and competition,* 2018.

[159] Non-resolicitation clauses in contracts between DCTs and suppliers require DCTs not to contact customers who have purchased a supplier's product from that DCT (in respect to the same product type) for a certain period.

[160] CMA, *Digital comparison tools market study final report,* September 2017, page 32.

[161] For example the creation of LendersCompared following the Competition Commission's market investigation into home credit, where it found that PCWs were unlikely to emerge spontaneously because of the perceived lack of commercial incentives.

[162] See the Open Up Challenge webpages for further details.

Automatic switching services or 'concierge' services

6.39 Concierge services (also known as automatic switching) take the use of data sharing further to help understand consumers' requirements, offer them more proactive help and act on their behalf.

6.40 Concierge services, which are relatively new, offer something closer to a one-stop-shop for identifying suitable deals and moving customers on to them. Some will not only switch consumers to a new supplier but will, if authorised to do so, continue to monitor offers and automatically switch consumers to a new tariff or supplier where beneficial.

6.41 By taking action on behalf of consumers, such services can take away much of the hassle and stress that can often act as deterrents to switching. As they greatly reduce both the time and effort required to manage contracts, concierge services can add particular value for inactive consumers affected by the loyalty penalty. Customers only need to make one decision – to sign up to a service – rather than requiring perpetual vigilance to ensure they are on the best rate for them.

6.42 Concierge services are likely to be most relevant where suppliers' marketing strategy is to offer low initial prices/high rewards which default at a later date to a higher price/lower reward, or which gradually rise over time (ie price walking, as described in chapter 2).

6.43 Where this model has been adopted by suppliers, consumers may forget, not notice or not have time to take action if subsequent deals could be better elsewhere. For these reasons and particularly where they are combined with smart data, we believe concierge services have potential to be effective in tackling the loyalty penalty. They could be especially beneficial to time-poor consumers.

6.44 However, there are groups of consumers who may be more reluctant to allow third parties to manage services for them. Consumers on low incomes, for example, may need or want to keep tight control over their finances.[163] Some may also be worried about being switched onto a supplier or product that does not meet their needs. However, some of these concerns may diminish as these services become more established.

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[163] BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018.

Switching services

6.45 Intermediary switching services allow consumers to switch providers more easily and quickly. They help consumers to manage the switching process once they have decided to switch and identified their preferred new supplier. Switching services seek to encourage higher levels of switching by reducing the time it takes to switch and making the process more reliable and less risky.

6.46 'Pure' switching services such as the Current Account Switch Service (CASS) and the Cash ISA Transfer Service operated by BACS,[164] perform the process of closing a consumer's existing account and opening and 'onboarding' to the new one. Ofcom has also implemented schemes to make it easier for consumers to switch in mobile[165] and parts of the broadband[166] market.

6.47 Switching services are likely to be of particular value in markets where the switching process is complex or daunting and/or where the costs or inconvenience of something going wrong are significant. In such markets the provision of a guarantee of a safe and swift transfer, such as that offered by CASS, is likely to be a useful element in lowering the barriers to switching.

6.48 However, switching services do not help consumers all the way through the switching process. They handle the last phase, the mechanics of closing the account with the current supplier and onboarding with the new one. But switching services do not provide an assessment of alternative suppliers or products and, where there are low levels of engagement, are unlikely to be sufficient without accompanying measures.

The role of human intermediaries

6.49 Some consumers may be less able to benefit from the solutions that we have described earlier and are likely to require additional measures to help avoid paying the loyalty penalty. This is particularly the case for some vulnerable consumers, who may not have online access or be less confident in engaging online. In these circumstances, the availability of information and recommendations either in person or over the telephone can be an important accompaniment to any remedy.

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[164] See the BACS website, Current Account Switch Service and Cash ISA Transfer Service for further details.
[165] Ofcom, *Decision on reforming the switching of mobile communication services,* 2017.
[166] For details of the gaining provider-led switching arrangements for customers with suppliers using the Openreach network see the Ofcom website. See also the discussion of gaining provider-led switching in chapter 7.

6.50 Local advisory services, such as Citizens Advice, could be well placed to help in this regard and to ensure that vulnerable consumers are able to benefit from innovative technologies. For example, we believe that Citizens Advice could play a more active role in providing information to consumers in local bureaus or through online tools (for example web chat), including directing consumers to trusted intermediary services, or even potentially helping consumers to switch. Such an approach would help to extend the reach of innovative intermediaries to less active consumers, would provide a point of contact for such consumers to discuss queries or provide advice, and would help overcome some of the scepticism that exists around automatic switching.

6.51 The positive effect that human intermediaries have in helping consumers can be seen in markets where the provision of face-to-face information and recommendations is already more common. In the mortgages market, for example, consumers can talk to lenders directly about the products available to them, or they can speak to mortgage intermediaries.[167]

6.52 While there is still more to be done in the mortgages market,[168] it is nonetheless clear that consumers value being able to discuss options with experienced intermediaries and feel that they are able to make better choices as a result.[169]

6.53 The success of Ofgem's recent collective switch trial (described in detail in paragraph 6.57) in triggering action among previously disengaged customers also demonstrates the value of providing a point of contact with whom to discuss options. In addition to providing an online route to switching, the scheme enabled consumers to switch via telephone, whereby they could also talk through any specific queries that they had. The ability to talk through options with an intermediary appears to have contributed to the success of the scheme, with 71% of switchers via the intermediary using the telephone route (vs 29% who switched online).

Collective switching

6.54 Collective switching typically entails a third party negotiating a better 'group' deal and offering this to consumers. It may involve an intermediary signing up

[167] The FCA's interim report on its mortgages market study finds that, of those who have taken out a residential mortgage (or switched product) in the last three years and arranged this through a mortgage intermediary, 89% agree they understood their needs and 75% agree they got a better deal than they would have got on their own. FCA, *Mortgages market study interim report*, May 2018, page 28.
[168] The FCA's interim report on its market study observed links between more expensive mortgages and intermediaries that typically place business with fewer lenders, for example.
[169] Another example includes the provision of specialist advice to people with pre-existing medical conditions when seeking insurance. See FCA, *FCA challenges industry to improve access to insurance for people with pre-existing medical conditions*, June 2018, for further detail.

customers and then approaching suppliers to negotiate special deals. In its simplest form, a collective switch provider would then offer each member of the group the same single offer on an opt in or opt out basis.[170] More complex forms include offering more than one deal for customers to choose between.

6.55 Collective switching schemes go beyond other engagement measures, as they do not simply scan the market for better deals for their customers. They also try to negotiate exclusive deals by harnessing the bargaining power of a group.

6.56 Alternatively, an intermediary such as a PCW might be able to negotiate exclusive deals for visitors to its website. Comparison and switching services such as uSwitch, are able to negotiate exclusive deals across a range of markets, including mobile, broadband and energy.

6.57 Following the CMA's energy market investigation in 2016,[171] Ofgem recently trialled a collective switching exercise which, as we describe here, produced some encouraging results.

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[170] Centre for Competition Policy, *Collective switching and possible uses of a disengaged consumer database,* August 2017.
[171] CMA, *Energy market investigation: final report*, June 2016.

- Ofgem appointed Energyhelpline to negotiate a deal for 50,000 disengaged customers (who had been on a SVT for at least three years).

- Results show that 22.4% of customers in the trial switched vs 2.6% in the control group who received no information. Customers who switched to a new tariff saved around £300 on average.[172] Of those who received letters and switched as part of the trial, 2.6% chose another tariff with their existing supplier, and 19.8% chose a tariff with another supplier. Of those who chose a tariff with another supplier:

    - just over half switched to the collective deal negotiated by Energyhelpline;
    - a quarter switched to other providers or tariffs after getting their open market results when they contacted Energyhelpline; and
    - just under a quarter chose another tariff without using Energyhelpline.

- Results suggest that there are a number of factors which appear to have contributed to the trial's success, including:

    - offering a 'switching shortcut' (switch managed by Energyhelpline rather than the customer);
    - offering various routes to switch (telephone as well as online);
    - providing personalised projected savings calculations, without the customer needing to provide consumption or tariff data;
    - providing open market search results along with the exclusively negotiated tariff, helping consumers make an informed choice;
    - a well-designed multipart direct mail series comprising three letters: announcement, saving and reminder letters (including a clear deadline, to combat inertia); and
    - regulator endorsement, leading to greater trust and credibility.

6.58 The success of collective switching depends on the ability to aggregate consumers into groups with similar requirements. This enables the group to benefit from their collective bargaining power and to negotiate a better deal through the collective switch. Collective switching is therefore most likely to be effective in markets where customers have high levels of similarity. One example might be in the cash savings market where there is a limited set of product features and customer requirements, or potentially in broadband.

6.59 As is apparent in the Ofgem trial, collective switching schemes can be designed specifically to target previously inactive consumers and can benefit

[172] Excludes savings for customers who switched to deals without using Energyhelpline.

participants by acting more generally as encouragements to switch. Even where participants do not take the collective deal (as was the case for half of the switchers in the Ofgem trial), potentially because it does not represent the cheapest deal for them,[173] the communication around it can act as a prompt and motivate participants to move to other available deals.

Applicability to the five markets

Mobile

6.60 Ofcom has introduced various measures aimed at improving engagement in the telecoms market (see Annex C for further details on previous interventions).

6.61 Ofcom is currently consulting on its final proposals to require all providers to send an end of contract notification, which will include information about the provider's best tariffs. For bundled handset and mobile customers, best tariff information must include at least one SIM-only deal.[174] It also published a consultation on mobile handsets in September 2018 which discusses the potential for further transparency measures and intends to publish detailed proposals to take this forward in 2019.

6.62 The complexity of tariff offers in the mobile market can often make it difficult for consumers to compare deals accurately and find the most suitable offers for them. While information remedies have led to improvements for some consumers and there is valuable work taking place in this area already, there is more to be done to improve consumer awareness of the options available to them. For example, consumer engagement research conducted by Ofcom in 2018 found that a quarter of consumers on a mobile handset contract were unaware of the possibility of moving to a SIM-only deal at the end of their minimum contract period.[175]

6.63 Ofcom also found that some major mobile providers did not inform consumers of this option after minimum contract expiry.[176] A targeted campaign to increase awareness and understanding of SIM-only deals could be a simple and effective way of protecting out of contract mobile customers from the loyalty penalty. It could also complement Ofcom's proposals on best tariff information. We recommend that Ofcom consider and test how information

[173] This may be the case where, for example, supplier participation is limited to include only those with a minimum third party quality rating.
[174] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018.
[175] Ofcom, *Consultation on end-of-contract and out-of-contract notifications,* July 2018, page 25.
[176] Ofcom, *Consultation on end-of-contract and out-of-contract notifications,* July 2018, page 20.

remedies can be designed to increase awareness and understanding of SIM-only deals, including the potential for setting targets for providers in raising awareness of such deals.

6.64 Smart data solutions could also significantly help consumers in the mobile market by enabling them to access and share their usage history with PCWs and other trusted intermediaries. Innovative intermediaries could then recommend a product to consumers based on their volume of calls, texts and data use, as well as the signal quality in their home or areas where they most frequently make or receive calls.

6.65 Such a solution could be considered the ‘gold standard’ of data portability and may take some time to implement. Ofcom should consider whether it can build on the existing usage data disclosures that the major mobile providers already provide to customers and how this can be improved – for example, in terms of completeness, accessibility, standardisation and how it can be accessed by third parties such as PCWs.[177]

6.66 Ofcom currently has a programme of work underway looking at new ways to use data to benefit and help engage consumers, including how to implement data portability in telecoms, which we support.

6.67 Intermediaries can also provide a range of services for consumers in the mobile market, from simple notifications and reminders of contract end dates to more complex solutions, for example through the application of automatic switching technology to the mobile market. While this may present some challenges in telecoms,[178] we recommend that Ofcom consider how it can best support the development of commercial initiatives that can help consumers to switch, particularly in light of the potential benefits for vulnerable consumers.

6.68 It seems unlikely that collective switching would be effective in the mobile market. For this reason, we understand that Ofcom will focus on smart data and intermediary-based remedies to complement its current interventions.

Broadband

6.69 Various forms of intervention have been introduced in recent years to make it easier for consumers to engage in the broadband market. Ofcom’s proposed

[177] This would be similar to the work that is currently being taken forward by Ofgem to revise the Midata programme. The CMA recommended, following our investigation into the retail energy market, that the government revise the Midata programme to ensure customers can access their data electronically, in order to conduct an accurate cross-market comparison.
[178] For example, in terms of compatibility with the EU’s Common Regulatory Framework and the new EU Electronic Communications Code introduced in December 2018.

rules for end of contract and annual best tariff notifications (see paragraph 6.62) would also apply to fixed broadband services. Ofcom has also recently launched a review into price differentiation in the fixed broadband market as well as a consumer awareness campaign to help people get a better deal.[179] Further details on this review and other interventions in the broadband market can be found in Annex C.

6.70 The broadband market is characterised by moderately diverse customer requirements, with providers offering varying levels of quality and download speeds. It is often sold as part of a bundle, usually with landline and often with pay TV and other ancillary services.

6.71 As with the mobile market, we consider that smart data solutions, particularly when used by concierge intermediaries, can and should be harnessed in broadband as this could be of great benefit to consumers.

6.72 We recommend that, as part of its engagement with the Smart Data Review, Ofcom consider how open APIs can be used to improve outcomes for longstanding consumers in the broadband market.[180] This could include, for example, enabling PCWs to access provider data on broadband speed and quality in different areas. This would allow consumers to make much more useful product comparisons than they can at present.

6.73 To maximise opportunities for intermediary services, Ofcom should also consider whether it would be feasible to require providers to hold consumers' usage data in a standardised, easily portable format and to make such data available through APIs to providers of DCTs.

6.74 While we expect there may be some challenges, there are features of the broadband market which may make it easier for some consumers to make use of concierge services, for example where they are switching within the Openreach network. Concierge services, which can assess which deals best match the needs of individual consumers, can potentially be a valuable supplement to the existing gaining provider-led switching process within the Openreach network, which makes the switching process easier once a consumer has identified their preferred new provider. We encourage Ofcom to consider how it can create favourable conditions for the development of innovative business models.

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[179] See the Ofcom website for further details on the Boost your Broadband campaign.
[180] We understand that Ofcom will be releasing two APIs, making connected nations fixed and mobile coverage data available at a premise level on a request by request basis. Providing wider access to this data can have significant benefits, for example by allowing consumer facing websites and apps to present coverage data within their own offerings and services. Ofcom's Boost your Broadband website also includes a broadband availability checker.

6.75 It is also possible that a collective switching service could be viable in the broadband market. We recognise that consumers' broadband requirements are variable but note that almost a third of UK households purchase broadband as part of a dual-play package with landline services.[181]

6.76 While there is a degree of heterogeneity in customer requirements (for example choice of broadband speeds), a carefully designed collective switch offering may be able to overcome this challenge. If a sufficient number of customers' requirements could be aggregated to the more commonly used packages of components and service levels, a collective switching service may be possible and beneficial.

6.77 To be viable in the broadband market, a collective switching service would also need to collect information on the availability of different broadband services in specific locations, to ensure that consumers were only presented with relevant offers. The use of smart data could enable a collective switching service to access this information, potentially overcoming some of the searching costs (regarding technical constraints) that can make engagement in the broadband market difficult.

6.78 We also note that some switching services are able to negotiate exclusive deals with providers for customers of broadband packages. Such deals are similar in principle to a collective switch.[182] We are aware of exclusive deals that are negotiated in this way for dual-play as well as for triple-play packages. Therefore, we consider that there may be scope to extend collective switching to more complex broadband packages.

6.79 Given the success of the recent Ofgem collective switch trial, we recommend that Ofcom review the feasibility of collective switching in broadband as part of its work in that market.

Cash savings

6.80 There have been various attempts to improve outcomes for longstanding consumers in the cash savings market. Some of the key interventions are summarised here, with more detail provided in Annex D.

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[181] See Annex C. Customer usage of such packages is not as complex and diverse as where triple-play (including pay TV) (31% of UK households) or quad-play (adding mobile) (5% of UK households) packages are purchased.

[182] By understanding what products and services consumers are searching for on their websites, switching services are able to identify where large groups of individuals are searching for similar packages. This information can then be used to negotiate exclusive deals that can be offered through the website of the switching service.

6.81 In December 2015, the FCA introduced a package of remedies, including various disclosure and switching remedies.[183] In addition the FCA proposed a 'switching box' and a 'return switching form' to make the switching process less burdensome. Results from trials, however, showed that these interventions would not be sufficient to change consumer behaviour to any material degree.

6.82 The FCA published a Discussion Paper on price discrimination in the cash savings market in July 2018 which set out various further options. These ranged from remedies to improve consumer engagement (by improving the previous trialling of the 'switching box') to remedies which focus on controlling outcomes. It is currently deciding whether to take any proposals forward.

6.83 Based on the evidence gathered to date, the FCA notes that demand side remedies are unlikely to address the harm caused to longstanding customers in the cash savings market.[184] We agree that there is a need to consider other remedies, including pricing regulation which is discussed in chapter 8.

6.84 We also see some potential for smart data together with the market development of concierge services as a potential remedy to the loyalty penalty in cash savings. Such services would track the returns being earned from an existing account and compare them with those available from others. They could, if instructed and subject to the rules on anti-money laundering (AML) and know your customer (KYC), move money from one account to another.

6.85 We recognise that to have maximum impact this remedy would require intermediaries to have read/write access to customers' cash savings accounts. However, the data sharing provisions of the revised Payment Services Directive apply only to payment accounts and while some cash savings accounts are also payment accounts, not all are.

6.86 We recommend that, as part of the Smart Data Review process, government and the FCA consider whether and, if so, how, the principles of Open Banking could be applied to cash savings. Given the work that has already been undertaken, the cost of adapting the Open Banking API, data and security standards to savings products should be relatively modest.

6.87 Services already exist which 'sweep' surplus cash out of current accounts to a (higher) interest bearing account. Open Banking technology, together with the emergence of intermediaries, including banks themselves acting in this

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[183] Including for example remedies such as a standardised summary box, trialling the publication of data on the lowest-paying interest rates and improved switching within a provider.
[184] FCA, *Discussion Paper on price discrimination in the cash savings market*, July 2018, page 18.

capacity, makes such services likely to be feasible from a technical and regulatory perspective.[185]

6.88 We also consider that, because of the relatively limited range of consumer requirements in the cash savings market, collective switching could have potential in this market. While consumer decisions are unlikely to be solely driven by the interest rate offered,[186] the variation in product offerings and requirements is not as diverse as, for example, in the mobile market.

6.89 We recognise that taking forward collective switching would not be without its complications.[187] However, we recommend that the FCA consider the lessons learned from Ofgem's recent trial and consider the application of collective switching to the cash savings market.

Home insurance

6.90 A number of engagement interventions have been made in the home insurance market. In particular in 2014, the FCA launched a large scale trial[188] to assess disclosure improvements to engage consumers at renewal. Of the disclosures tested, the inclusion of the last year's premium was found to be the most effective in increasing engagement.[189]

6.91 The FCA introduced new rules from April 2017, applicable across general insurance renewals, requiring various disclosures by firms to encourage consumers to shop around, including disclosing last year's premium at each renewal. For more details on these and other interventions in the home insurance market see Annex D.

6.92 In October 2018, the FCA published its terms of reference for a market study into general insurance pricing practices.[190] The market study will examine pricing practices in retail home and motor insurance.

6.93 The results of the FCA's testing of disclosures are encouraging and demonstrate the impact that well-designed and well-timed information remedies can have in prompting more consumers to shop around.

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[185] Though might, if adopted on a large scale, give rise to concerns from a prudential regulation perspective.
[186] Consumers may consider additional factors in choosing a savings product (for example risk, access to savings, the convenience of having products with the same provider).
[187] For example, the difficulties that banks may face in onboarding large numbers of clients over a short period and their obligations as regards AML and KYC.
[188] The trial was carried out with over 300,000 customers from one home insurance and two motor insurance providers.
[189] 11 to 18% more consumers switched or negotiated their home insurance policy. FCA, *Increasing transparency and engagement at renewal in general insurance markets,* December 2015, page 10.
[190] FCA, *General insurance pricing practices: terms of reference,* October 2018.

6.94 As noted in paragraph 6.9, we consider that there may be scope to further strengthen the rules on provider disclosure. A requirement to disclose the cumulative impact of price changes since a customer's first insurance premium, for example, could act to draw greater attention to the need to switch. In our view, such a disclosure is worth further consideration, and could complement the FCA's current rules on additional disclosures for existing customers.

6.95 Given the requirement for consumers to provide extensive information to potential providers, there is also potential for the application of smart data solutions in the home insurance market. These new technologies would allow consumers themselves or intermediaries acting on their behalf to share data with potential suppliers and generate bespoke quotes.

6.96 Concierge services could automatically switch customers if subsequent premiums rose above the new customer offer price of other insurers. As the use of smart data becomes more sophisticated, the development of open APIs could enable intermediaries to access third party product performance metrics, including quality ratings. They could also take account of these in switching decisions to guard against the 'hollowing out' of insurance products – for example, by only switching consumers to products with an agreed minimum service quality rating or pay-out ratio.

6.97 While the Smart Data Review is ongoing, the FCA should consider whether it can implement 'semi-smart' solutions in the short to medium term that could be beneficial for consumers. By requiring the standardisation of information that home insurers ask customers, for example, intermediaries could capture customer data and use that information to inform individual customers of 'best buy' products. Customers could easily compare this information against their current provider's renewal quote to assess whether they should switch.

6.98 We recommend that the FCA continue its focus on developing intelligent nudges that can trigger consumers to act. In doing so, it is important that the FCA consider how providers may be able to improve the way that they communicate information about insurance products to be as clear as possible for all consumers,[191] and particularly bearing in mind the needs of vulnerable consumers.

6.99 Research suggests that, although consumers often view receiving prompts favourably, they find the insurance market the most difficult to understand of

[191] We are aware of significant work already undertaken at EU level to standardise the way that basic information about insurance products are presented to consumers. See the FCA webpages on the Insurance Distribution Directive for further details.

the five markets identified in the super-complaint, and the terminology to be particularly complex. This is likely to lead to disengagement by consumers and can further entrench vulnerable consumers' mistrust of suppliers.[192]

6.100 In our view, the nature of the home insurance market (and insurance products more generally) would make collective switching difficult to achieve.

6.101 We encourage the FCA to be bold in its market study in its consideration of possible remedies, where lighter-touch engagement remedies may not be sufficient. Our views on regulating prices are discussed in detail in chapter 8.

Mortgages

6.102 In recent years, the FCA has introduced various transparency remedies to help mortgage consumers at different stages of the decision making process.[193]

6.103 The FCA's mortgage market study, which published its interim report in May 2018 found that, overall, the mortgage market is working well in many respects. In particular:

- the market has high levels of consumer engagement: currently over three-quarters of consumers switch to a new mortgage deal within six months of moving onto a reversion rate; and
- consumers who use an intermediary do so for a range of reasons, in particular valuing their experience and expertise.[194]

6.104 As part of its ongoing market study, the FCA is consulting on a number of further engagement measures, which we discuss here. Further details on interventions in the mortgage market can be found in Annex D.

6.105 The generally high levels of switching that can be observed in the mortgage market suggests that consumers, on average, are more engaged in this market than in the other markets identified in the super-complaint. However, there are still further improvements that could be made.

6.106 As part of the next phase of the FCA's market study, it is consulting on helping consumers to assess and choose an intermediary and challenging the industry to develop tools to help consumers in this regard. Given the

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[192] BritainThinks, *Getting a good deal on a low income: qualitative research conducted with vulnerable consumers on behalf of the Competition and Markets Authority*, December 2018.
[193] This includes requiring firms to provide a standardised Initial Disclosure Document, setting out key information about the service that customers should expect, and the provision of a Key Facts Illustration, detailing personalised product information, early in the mortgage sales process as well as at the offer stage.
[194] FCA, *Mortgages market study interim report*, May 2018, page 4.

importance of intermediaries to the market, we strongly support this approach by the FCA.

6.107 The FCA is also consulting on lenders making information available to intermediaries. This would make it easier for intermediaries to more quickly and easily identify the mortgages that a consumer may qualify for. We support the FCA's proposed work with industry which could develop new and innovative tools that can make it easier for consumers to engage in the market and find the right deals for them.

6.108 In addition, applying smart data principles and empowering consumers to give intermediaries access to their information can add further value in the mortgage market, for example by speeding up affordability assessments.[195] We recommend that the FCA also consider how data portability can benefit mortgage customers as part of its engagement with the Smart Data Review.

6.109 Given high switching rates and other factors in mortgages, it seems unlikely that collective switching would be effective or practicable in the mortgage market.[196]

Recommendations

6.110 In this chapter we have identified new and innovative approaches which could increase engagement among some consumers and help them to switch to avoid paying the loyalty penalty.

6.111 Well-designed nudges can have a positive effect on some consumers, and testing and trialling should continue to help regulators fine tune interventions in this area. In particular:

(a) in insurance, we recommend that the FCA continue to develop renewal disclosures and explicitly consider the needs of vulnerable consumers, who can find terminology in the insurance market complex. To complement its existing rules on renewal disclosures, we also recommend that the FCA consider whether these can be strengthened by including additional information (for example cumulative impact of price rises); and

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[195] The Australian Competition and Consumer Commission's report on its residential mortgage products price inquiry, proposes the adoption of a portable data solution as part of the Consumer Data Right programme, to enable borrowers to share their financial data with prospective mortgage lenders.

[196] A collective switch was trialled with 40,000 mortgage holders in Australia in 2011. We have not examined this trial in detail but note that the switching rate was low (at best 5%) with 2,000 individuals entering into detailed discussions with banks. In our view, the necessity of subsequent individual discussions highlights the difficulty in designing a collective switch for mortgage holders. More detail can be found in Centre for Competition Policy, *Collective switching and possible uses of a disengaged consumer database*, August 2017.

(b) in mobile, low levels of awareness and understanding of SIM-only deals could be tackled through a targeted campaign which could complement Ofcom's proposals on best tariff information.

6.112 Smart data can be transformative in how consumers engage with markets. Open Banking is a good start and shows what can be achieved. Regulators in other markets, the CMA and government need to work together to ensure that consumers in other regulated markets benefit from new data-driven technologies, particularly in telecoms where it would be highly beneficial.

6.113 However, we also recommend that regulators consider where semi-smart solutions can be introduced more quickly or maximised to help tackle the loyalty penalty, such as in insurance and mobile, to help people make quicker and easier comparisons.

6.114 Intermediaries can be leveraged to support switching and can be particularly valuable for vulnerable consumers, who may require additional support in searching and switching to better deals (see chapter 3 for more detail). In particular, we recommend that:

(a) the FCA explore how intermediaries can continue to benefit the home insurance market;

(b) as part of the Smart Data Review, government and the FCA consider the feasibility of extending the data sharing requirements of Open Banking to cover savings accounts; and

(c) Ofcom review how it can create favourable conditions for the development of innovative intermediaries in the mobile and broadband markets.

6.115 The availability of personal support should also not be underestimated. Local advisory services can play an important role in this regard where consumers reach out to them for help. Organisations such as Citizens Advice could potentially play a more active role here and we recommend that government consider this further.

6.116 Ofgem's collective switching trials are very promising and show that collective switching can be successful in increasing switching rates among long term inactive customers. We recommend that both Ofcom and the FCA review carefully the results of the trial, applying lessons to their own interventions and consider its feasibility in broadband and cash savings.

7. Stopping harmful business practices

- Business practices across a wide range of markets can hinder consumers from engaging, switching or getting better deals - such as making it harder to exit a contract or to find information about deals. These can have especially negative impacts on consumers who may be vulnerable.

- We have set out a number of clear principles to stop these unacceptable practices, including:
    - people must be able to exit as easily as they can enter into a contract;
    - consumers should be aware and properly notified of the renewal and any price changes in good time;
    - auto-renewal onto a new or fixed term should generally not be used;
    - auto-renewal should generally be on an opt in basis upfront;
    - switching should generally be managed by the gaining supplier; and
    - exit fees should not be used after any initial fixed or minimum term.

- We have opened enforcement cases to investigate whether there have been breaches of consumer law in the anti-virus software market.

- We will undertake further work to identify targets for enforcement action as part of a wider consumer law compliance campaign.

- Many of the practices identified and our recommendations can be addressed through existing consumer law or regulator action. But we will also assess the case for legislative change to ensure the core principles are applied, alongside new powers for the CMA to seek substantial fines where law is breached.

Introduction

7.1 This chapter considers the range of harmful practices which businesses use to hinder consumers from engaging, switching or getting better deals, such as making it hard to exit a contract or to find information about deals. Such practices have been described as 'sludge' - practices which 'appear intentionally designed to discourage behaviour which is in the consumers' best interests'.[197] Where such practices are combined with price rises,[198] this can make it more likely that customers stay with their existing provider and as a result, may pay a loyalty penalty (rather than switch or negotiate to better

[197] Richard Thaler, *Nudge not sludge*, Science Magazine, Vol. 361, Issue 6401, page 431.
[198] Or in cash savings, a reduced interest rate.

deals). These practices occur in a broad range of markets (both regulated and non-regulated).

7.2 This chapter is structured as follows:

a) the different types of harmful business practices and how these could be addressed:

i. practices around auto-renewals and roll over processes;
ii. lack of choice over auto-renewal;
iii. difficulties in switching or cancelling a contract;
iv. unfair or disproportionate exit fees; and
v. making it hard for consumers to access the information they need;

b) what can be done to stop these harmful practices in current consumer law; and

c) conclusion – setting out core principles for businesses.

7.3 The laws and sectoral rules that apply to these practices are largely principles-based, and therefore can be applied flexibly to tackle emerging problems. We describe the relevant legal framework and key sector-specific rules more fully in Annex F. In some areas there has been enforcement to tackle these issues in the five markets highlighted by Citizens Advice - mobile, broadband, cash savings, home insurance and mortgages - and in other similar markets. However continued action is required, both within the five markets and across the rest of the economy, to ensure businesses are fully held to account.[199]

7.4 Although these practices have an impact on all consumers, they can have an especially negative impact on people who may be vulnerable, such as the elderly, those with mental health problems, on a low income or with low levels of education. Such consumers can face additional challenges to engaging in a market and may find the process of switching providers daunting (see chapter 3 for more detail). Areas of vulnerability which are particularly relevant in this chapter include:

- lack of or poor digital skills which make it hard for people to access information sent only by email or uploaded to an online account;

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[199] Action the CMA or Trading Standards can take includes civil enforcement to change suppliers' behaviour and potentially to secure redress under Part 8 of EA02, and criminal prosecution of offences under the CPRs. Regulators can also address business practices using their own consumer enforcement and regulatory powers, targeting the sectors they cover. In addition, individual consumers may have private rights of redress under the Consumer Rights Act 2015 (CPA) or the CPRs (see Annex F for further details).

- visual impairment which makes reading small print and lengthy terms and conditions difficult;
- cognitive difficulties or poor English language skills which can mean people to struggle to understand the effect of an exit fee or realise the significance of any minimum term; and
- mental health problems which can mean individuals become overwhelmed with information and can disengage completely as a coping mechanism or cannot use the telephone to contact suppliers.

7.5 This chapter is informed by the evidence contained in the super-complaint, supplemented with complaint information from the regulators and relevant ombudsmen, stakeholders (including insights directly from consumers), and desk research. We also draw on legacy work by the Office of Fair Trading, particularly previous work on principles for the use of continuous payment authorities and the report on ongoing contractual relations,[200] and commissioned qualitative research with vulnerable consumers.[201]

Summary of harmful business practices

Practices around auto-renewals and roll over processes

7.6 A recurrent theme that we have seen across a number of markets,[202] relates to what happens when the initial deal that a consumer originally agreed to expires and the contract is either renewed (such as a subscription beginning again for a further year) or the individual is rolled onto a different deal (such as a fixed rate savings account reverting to a low rate).[203] Where the price increases, it is possible that consumers could get a better deal elsewhere. Sometimes consumers may not want to continue receiving the product at all.

7.7 Auto-renewals and roll overs can be beneficial for consumers who want to ensure they continue to receive a product or service or where it is easier and more convenient than repeatedly purchasing it. However, we have found in some circumstances these can also lead to consumer harm, for example:

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[200] OFT, *Key issues in ongoing contracts: a practical guide,* June 2013.
[201] The examples included in this chapter are illustrative of the practices of concern. The inclusion of an example does not imply the practice is prevalent across the market concerned or that all practices described occur in all markets.
[202] Mortgage contracts are long term products that operate generally over the course of 25 to 35 years and do not renew or roll over in the sense described in this chapter. Consumers may view the expiry of the fixed rate element of the mortgage contract as a roll over onto the reversion rate.
[203] In telecoms, auto-renewal refers specifically to customer contracts being renewed into a new minimum term (see further at paragraph 7.15) and roll over describes the customer reverting to a rolling 30-day contract while continuing to receive and pay for services.

- there is sometimes insufficient transparency and warning about price increases;
- where customers are locked into a fresh minimum term on renewal or roll over, possibly with fees for early exit; and
- when it is difficult for consumers to prevent the renewal or roll over or there is insufficient warning about it.

7.8 These problems can mean that consumers find themselves trapped in a contract that they did not consent to and are receiving goods or services they did not want or paying a price that is higher than the initial or previous contract. This has significant potential to exploit consumers' trust in suppliers, especially when combined with repeated price rises.

Unexpected and/or continual price rises

7.9 We have seen multiple complaints from consumers who on renewal, the price they are being asked to pay has gone up. Sometimes this comes as a surprise, and it is a particular problem where the individual has not expressly agreed to it, is unaware, or not warned in advance. In some cases, where suppliers continually raise prices year on year the longer a customer stays (price walking), this can lead to very significant increases from the original price.[204] We consider price walking and how to address it, in chapter 8.

7.10 We would generally expect businesses to obtain consumers' agreement upfront to the potential change, as well as setting out how the price might change (by reference to clear criteria that consumers can understand).[205] We are concerned where price rises are unrelated to changes to the cost of supplying a service (and risk in relation to insurance), and that this may not be fair to consumers. We also think that consumers generally would not expect their supplier to set their prices in this way.

7.11 Where a change is unexpected, or consent has not been obtained, we think that generally consumers should be asked to explicitly agree to the new terms. That is, their contract should not be extended automatically on terms which increase the price.[206] It is also important that suppliers provide consumers with sufficient notification and clear information about changes in advance to inform their decision of whether to renew.

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[204] The inverse is where the price paid by the supplier is reduced - as in cash savings.
[205] Where telecoms contracts are changed mid-term, the provider is required under Ofcom's general conditions to notify the customer and to allow them to exit the contract without penalty if that change is of 'material detriment' to the customer (general condition C1.6). The FCA is publishing guidance on the fairness of variation terms in financial services consumer contracts on 19 December 2018.
[206] The fact that a consumer may be able to switch does not prevent a price increase from being unfair.

7.12 From 1 April 2017, insurers have been required to send a renewal notice to customers which sets out the renewal premium and last year's premium, to enable easy comparison.[207] However, we have seen reports of firms failing to meet this obligation by either not providing the notice or by including inaccurate premium information.[208] The FCA has recently launched a package of work looking at pricing practices in general insurance, including a market study looking at home and motor insurance.[209] The FCA is also conducting an evaluation of its recent rule on renewal notices, aiming to increase transparency and engagement at insurance renewal. It has also taken action in relation to firms that are potentially not complying with the rules.[210] Chapter 6 considers information remedies in more detail.

> A customer with dementia had the same home insurer for 15 years and was auto-renewed each year. The insurance company also told him that he was being given discounts for his loyalty and lack of claims. However, over this time his premium rose from £200 to £1,499. Equivalent cover was available online for £150.

7.13 Ofcom has recently published a consultation on requirements for communication providers to send end of contract notifications to their customers, with information included on the 'best tariff' available to the customer for their service.[211]

Locking consumers into a new fixed term

7.14 An automatic renewal onto a new fixed term is unlikely to be appropriate for most products or services. We would always expect businesses to be able to clearly justify why a minimum period is in a customer's interests or otherwise essential to service provision. Generally, we would expect any continuation of service to be on a rolling basis, which could be terminated on no more than 30-days' notice, unless otherwise agreed.

7.15 In cases where consumers would expect a product or service to continue after the end of the initial minimum term, this should be made clear upfront to give consumers the opportunity to agree or stop the renewal when first contracting.

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[207] FCA, *Insurance Conduct of Business Sourcebook (ICOBS)*, rule 6.5 (renewals).
[208] FCA, *Admiral agrees to contact customers who have been given inaccurate information in renewal documents*, 16 June 2017.
[209] FCA, *General insurance pricing practices market study,* 31 October 2018.
[210] FCA, *Insurance firms still failing to meet FCA general insurance renewal rules*, 3 April 2018.
[211] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018. Ofcom is also proposing that providers will be required to send this 'best tariff' information to customers annually once they are out of contract. See Annex C for further details.

Even where continuity of supply is in a consumer's interests, they should have the option of stopping it. We discuss this in the next section.

7.16 Communications providers are prohibited from automatically renewing customers for a further fixed term contract unless the customer has expressly consented.[212] In practice this means customers generally roll onto a new 30-day contract once their initial contract ends. This ensures continuity of service while giving the customer a chance to search and switch if they wish to. However, we have heard that some mobile providers (and third party sellers) circumvent this rule by inviting customers to 'upgrade' but failing to make clear that they are committing to a new two-year contract. Such conduct would likely contravene Ofcom's regulations.[213]

7.17 In the insurance market, a number of consumers report experiencing difficulties. We have seen complaints of people being locked into a fresh 12-month policy, with fees payable for changes and early termination, when they would have preferred to amend their cover, stop it altogether, or switch to another provider.[214] In several cases these renewals were combined with insufficient notice, and premiums being taken before the expected renewal date. It is possible that some firms are not complying with the requirement to give a 14-day cooling off period or providing notice of the renewal in a manner which is not reaching some consumers. We note that the FCA is considering the information that firms provide to consumers on renewal as part of its market study on general insurance pricing practices. We recommend it examines how insurance renewal is working in practice, as part of this.

7.18 Consumers complain most frequently about the penalties they need to pay on auto-renewal. One of example of this would be, while an insurance customer can usually give notice to terminate their cover as long as they have not yet made a claim and receive a pro-rated refund of their premium (outside of a cooling off period), they may still face administration fees of sometimes £50-75. We consider exit fees later in this chapter.[215]

Difficulties preventing auto-renewal and insufficient notification

7.19 Businesses should warn customers before their contract is going to auto-renew or roll over. They should also provide appropriate information to enable

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[212] Ofcom's general condition C1.3.
[213] This may also breach Ofcom's general condition C1.3 because it requires that customers give their 'explicit consent' to upgrade. In addition, C8.5 requires mobile providers to inform customers at the point of sale what their contract duration is.
[214] FCA ICOBS rule 7.1.1 requires a minimum 14-day cancellation or 'cooling off' period, allowing the customer to cancel without penalty.
[215] When we refer to exit fees, we mean additional fees that do not reflect supplier costs.

customers to take action if they wish to prevent this. This notification should be sufficiently in advance to give customers time to compare deals.[216] This is especially important if any aspect of the contract is being changed or the opt in process was at the start of a contract, as the customer's needs or wishes may have changed, or they may simply have forgotten.

7.20 However, we have seen instances where consumers do not have sufficient warning about renewal or face unnecessary difficulties in preventing their contract being renewed or rolled over. Examples include:

- not being clearly informed that their renewal notice would only be made available in an online account;
- receiving no prompt or reminder that renewal was going to take place;[217]
- the supplier taking payment for the next period at the end of 10 months, when 12-month contracts are the typical term for the product; and
- the renewal notification being sent to an old and unused email address as supplier records have not been updated.

7.21 We have also seen practices across non-regulated markets, which have the effect of overruling the consumer's stated intention not to agree to auto-renew, such as:

- suppliers changing the customer's selection after they have opted out of auto-renewal;
- regular, irritating onscreen pop ups to prompt users to auto-renew;
- payment of monthly instalments by direct debit being made conditional on auto-renewal; and
- complaints that payment is taken even though the consumer opted out of auto-renewals.

7.22 Consumers can also experience difficulty in contacting their supplier to prevent auto-renewal, which can dissuade them from cancelling. We discuss difficulties switching or cancelling a contract in the next section.

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[216] FCA ICOBS, rule 6.1.5 requires firms to ensure that a customer is given appropriate information about a policy in good time. Industry standard is to send a renewal notice six to eight weeks before renewal. In cash savings, FCA Banking Conduct of Business Sourcebook (BCOBS) rule 4.1.2 requires a pre-contractual explanation in a summary box explaining what happens at the end of a fixed term. Ofcom is currently consulting on a requirement for communication providers to send end of contract notifications with information on the 'best tariff' available to the customer for their service, which will implement requirements under the EU Electronic Communications Code (EECC). See Annexes C and F for further details on the EU Code and this consultation.
[217] Failure to provide renewal notice in good time before renewal would constitute a breach of FCA ICOBS rules 6.1.5R and 6.5.1R.

Stopping harmful business practices around auto-renewals

7.23 In order to address these practices, we consider that it is necessary, across all markets, for consumers to have greater control of the renewal process. In particular:

- suppliers should provide customers with an easy to find and use function to stop the roll over or renewal at any time;
- consumers should be aware and properly notified that the contract will renew, and of the contract terms (ie through notifications made sufficiently in advance). Suppliers should be able to demonstrate that customers are aware of the renewal;
- any changes to the price or the product or service should generally not be made without consumers' agreement, either based on clear information in the original contract, or a new agreement at the time of the renewal;
- renewal onto a fresh minimum term should not generally be used and only where clearly in the customer's interests; and
- consumers should be given a cancellation right and have an easy means to exercise it after the renewal.[218]

Lack of choice over auto-renewal

7.24 Customers should generally be presented with a clear and prominent option to enter an initial contract without needing to agree to roll over or renew.

7.25 Consumers may wish to receive certain products automatically, for example insurance products which may be legally required (eg motor insurance), or products such as magazine subscriptions or pay TV which the customer considers desirable to continue. Generally, suppliers should not assume that this will always be the case and regardless of the form of the contract, should not use negative options to automatically extend contracts. Consumers should be given the opportunity to opt in to being auto-renewed.

7.26 It is especially important that auto-renewal is not abused where the consumer would not expect to continue receiving the product at the end of the initial contract. For example, where it is clear that a consumer is not using a product, suppliers should have systems in place to prevent continued auto-renewal and should seek fresh consent, rather than continuing to charge

[218] As a renewal generally consists of a new contract, a cancellation right exists for distance contracts under the CCRs and for banking products, under the FCA's BCOBS, although some products such as fixed rate savings products and products linked to market performance do not have a cancellation right (rule 6.1). Similar rights exist for insurance products under the FCA's ICOBS. In telecoms, the EECC includes provisions on renewals. See Annex F for more detail.

customers for a product they are not using. We have seen a wide range of different examples of this latter practice across a number of different markets.

> One individual's car insurance was auto-renewed even though the insurance company knew that his car had been stolen, had already paid out on this claim, and would need fresh information in order to continue to provide cover.

7.27 In some regulated markets, such as energy and telecoms, continued service is critical and there may be clear reasons why auto-renewal is necessary to ensure services are not cut off or ended unexpectedly. In such cases, it is sufficient for suppliers to make very clear that supply will continue at the end of any initial fixed period or to offer other protections that customers will not experience the harmful practices that can accompany auto-renewal.

7.28 In these types of markets, there is no auto-renewal after a discounted fixed period on a contract ends - as these contracts have an indefinite duration. However, it is important that customers have agreed and are alerted to the non-discounted price that will be charged after the initial rate has ended.[219]

7.29 Often the reason suppliers are able to auto-renew is because they are in control of taking payment by virtue of an arrangement such as a continuous payment authority (CPA). This is a mechanism which authorises businesses to take recurring payments from a customer's bank account or credit card whenever the business considers it is due. It should also allow the customer to cancel via their bank and recover funds paid in error.[220] Without a CPA, for a consumer to continue receiving a product they would need to consciously agree to new terms of supply.

7.30 While beneficial, the use of CPAs is open to abuse. Consumers can get caught in a 'subscription trap' and face a situation where their supplier has increased payments directly with their bank.[221] This is especially problematic where suppliers continue to take payments even when the consumer has instructed them to stop. Card issuers must refund these payments and any related charges immediately. Where banks fail to prevent payments being

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[219] Where the supplier finds it difficult to explain what price will be charged at the end of the minimum period, this practice is likely to be problematic under consumer law, for lacking transparency.
[220] The OFT previously issued principles about the proper use of CPAs, which stated that businesses should not fail to highlight, at sign up or roll over (or both), where the subsequent tie in period is on less favourable price or other terms than the first, fail to make clear that the contract and payment is continuous, require unduly complicated procedures for cancellation or opt out, or an unduly long minimum contract, or cancellation period.
[221] The government announced its commitment to tackling subscription traps in the Spring Budget 2017.

taken after the consumer has revoked authority, this is contrary to consumers' legal rights.[222]

Stopping harmful business practices around whether a contract auto-renews

7.31 In order to address these practices, we consider that it is necessary for consumers to understand what will happen at the end of a contract. While auto-renewals are important in many markets, the process must be properly agreed to. Consumers should generally be presented with a clear and prominent (and no less convenient) option to take the contract without auto-renewal, and businesses should not pressure them to agree to auto-renewal.

Difficulties in switching or cancelling a contract

7.32 We have heard a number of concerns from people about the difficulties they face in exiting contracts with their existing supplier, for example when they wish to stop receiving the product or want to change supplier. Ofcom found that 35% of customers who had switched in the previous two years reported 'cancelling your previous service' as a difficulty during the process.[223]

7.33 Where consumers fear or experience issues such as loss of supply, monetary cost, stress or inconvenience, this may lead them to stay with their existing supplier, even if they are unhappy with the overall service or they could get a better deal elsewhere. This increases the risk of such customers suffering the loyalty penalty and allows businesses to continue charging higher prices to existing customers.

7.34 While it can sometimes be complicated to change provider, we are concerned that businesses do not always do all they can to make it easy to switch and may make switching more difficult.[224] For example, we have seen evidence of customers:

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[222] Under the Payment Services Regulations (PSRs) 2017 section 67(3), customers can withdraw their consent to the execution of a series of payment transactions at any time with the effect that any future payment transactions are not regarded as authorised. Where an unauthorised payment is made by the bank, the consumer is entitled to a refund (section 74). Where a contract is entered into by distance means, the Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013 provides that all payments taken from a consumer must be expressly consented to - where they are not, it is likely that they are not authorised for the purposes of PSR.
[223] Ofcom, *Triple plan switching: online research main findings,* 2016.
[224] In 2016 Ofcom concluded an enforcement programme into cancellation arrangements, which was launched in response to concerns that providers were making it difficult for customers to cancel, including some of the practices highlighted in this section. As part of this work Ofcom also undertook a formal investigation into Sky's procedures, which looked at agent behaviours on calls with customers. This enforcement work resulted in providers making a number of improvements and changes to their procedures to make it easier for customers to cancel, and Ofcom has subsequently published guidance on its approach to investigating practices in this area.

- requiring customers to phone customer service to cancel or switch, when they were able to sign up in various ways (including online or by email), or use other onerous processes not required on sign up;
- having to contact the losing provider repeatedly to ensure the cancellation is registered or the switch initiated;
- having to chase both the losing and gaining providers to ensure the switch occurs at the right time and for the right service;
- losing access to their telephone and/or broadband service at the point of switching; and
- experiencing loss of important rights such as their phone number, email address, no claims bonus or other discount, and data, when trying to switch.

7.35 Some suppliers exploit these obstacles to impose even more barriers, for example by:

- not answering the phone or keeping customers on hold for long periods, or call centres operating at limited or inconvenient times;
- requiring customers to make repeated requests to switch/cancel or telephone contact to be followed up in writing; or
- training customer service staff or using scripts that encourage obstructive practices, or incentivising customer service staff to upsell (for example by paying commission). This makes it harder for customers to switch, or in effect means they have to threaten to cancel, to negotiate a better deal.[225]

7.36 We have seen examples of customers facing hour-long call waiting times to get through to a cancellation team and having no option to cancel online (despite having signed up online). In one case, a customer was given a response waiting time of two days, by which time his policy would have renewed. Some customers have been able to agree a contract via an online chat function but have had to contact a call centre if they want to cancel.

7.37 Customers have experienced call centres disconnecting calls, including after waiting for extended periods, as the call centre had closed. Consumers have also reported 'hassle costs' from being passed on to a number of agents and having to re-explain their issue or query a number of times. When attempting to cancel through call centres, some consumers - especially those who may be vulnerable - report facing unacceptable difficulties, such as being sold inappropriate products or having their instructions disregarded.

[225] Should this practice occur in insurance markets, it would likely not be compliant with the requirement to act in the customer's best interests under the Insurance Distribution Directive (further discussed in Annex F).

An elderly widow called her telecoms provider to cancel the service after her husband died as she could no longer afford it. The cancellation agent offered to transfer the contract to her name to keep a limited service. After hearing the cost, she declined as it was still too expensive. The agent confirmed the cancellation and said the new provider would confirm the switch. She re-contracted with a new supplier but four months later received a bill for £150, and another for £180. On enquiring, the agent confirmed the original contract had not been cancelled, it was now in her name and she could not cancel for four months. Despite being told she would be contacted, she was not and subsequently received a bill for £200.

Stopping the practices that make it difficult to exit or switch

7.38 Consumers should find it at least as easy to exit a contract as it was to enter. For example, where a supplier permits consumers to sign up online, the same facility should be offered to all customers to exit, without being required to speak to the supplier. Consumers should also have the flexibility to cancel in the way that best suits their needs and is practical given the subject matter of the contract. For instance, customers should be given the option to cancel a contract over the phone without having to speak to someone about available deals or offers. We expect suppliers to simplify the process of exiting a contract as much as practicable.

7.39 Customer service and exit handling also needs to improve, both by restricting call times and call waiting. Suppliers should be required to handle customer service and exit calls expeditiously and effectively, and invest sufficiently in staff, including in training and systems to make it a professional process.

7.40 Where it is necessary for the supplier to provide information or take action to enable switching, the switch should generally be managed by the supplier the customer is switching to (‘gaining provider-led switching’). This incentivises the provider to give the customer a good switching experience. They are also better placed to overcome any obstacles to the switch by the losing provider. This approach (or similar variants) is in place in some of the five markets already (see chapter 6 for some examples).

Unfair or disproportionate exit fees

7.41 Consumers also report facing unfair charges for cancelling a contract or leaving their existing supplier after a minimum term has expired (exit fees). An exit fee (when it is in addition to the supplier’s incurred costs) can be particularly harmful if it inhibits a consumer from taking action where the supplier has changed the deal in some way, or where the contract has been renewed onto a new minimum term without express agreement.

7.42 We have seen numerous examples of problematic exit fees. This includes fees that are disproportionately high, lack of clarity that exit fees are required because a new contract had been entered into and where the standard of service falls short but customers are still charged exit fees.

> When a customer who realised their mobile data speeds were insufficient attempted to cancel within their cooling-off period they were told they would have to pay a £150 cancellation fee if they wanted to keep their number and obtain a PAC

> One broadband customer wanted to cancel as they were not receiving broadband speeds they had expected and was told they could not exit without paying a contractual penalty. [226]

7.43 Unjustified exit fees make it difficult for customers to end their contracts and switch supplier. This can have a number of negative impacts. It can lead to customers paying more than they need to or continuing to receive a product they do not want or need. It also weakens competition between suppliers, as it makes it harder for another supplier to gain the locked-in customer's business. It is also very unfair to the individual faced with the fee.

Stopping the practice of unfair exit fees

7.44 In general, we consider there should be no exit fees after any initial minimum or fixed term, during any cancellation period, or in any situation where a supplier is not providing the agreed standard of service. Where a customer has rolled over and is, for instance, on a 30-day rolling contract, exit fees should not be applied if they subsequently wish to exit. Exit fees are often linked to the remaining term within a fixed term contract.

Making it hard for consumers to access the information they need

7.45 Consumers need access to relevant and timely information about products before they decide to enter into a contract, as well as at key points during the

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[226] This practice is explicitly banned by Ofcom through the broadband speeds Code of Practice – customers have to be given the right to exit, penalty free. Ofcom has an ongoing enforcement programme looking at exit fees in its markets, in particular to ensure that these fees are not excessive and are fair and transparent and it recently issued fines against Virgin Media and EE charging excessive exit fees. See Ofcom, *Enforcement programme into early termination charges*, June 2018. Ofcom, *Investigation into Virgin Media's early termination charges*, November 2018. Ofcom, *Investigation into EE's early termination charges*, November 2018.

contract and renewal. Suppliers can make it harder than necessary for consumers to get this information, which can lead them to make poor decisions and hinder them from exiting contracts. Chapter 6 discussed the effectiveness of information remedies to increase engagement. Here, we look at examples of poor practice: where businesses are failing to meet the minimum requirements expected of them and the impacts on consumers.

False or deceptive statements

7.46 Consumers are entitled to be given information which is truthful and helpful. They should not have to double check statements made by their suppliers. [227] It is therefore a problem when businesses:

- misrepresent the extent of a price increase over the previous year's price;
- give the impression that a customer is getting a 'good deal' for being loyal, when they are getting a worse deal (or at least no better deal) than is on offer to new customers;
- tell customers a deal on offer is the 'best' deal for them, when the salesperson has authority to negotiate a better deal if challenged;
- describe a renewal as an 'upgrade' when the consumer is simply entering into a new fixed term contract; or
- misstate the process needed to exit a contract.[228]

7.47 These practices appear to occur more frequently through direct selling by telephone. Consumers report being induced to renew or upgrade contracts by statements which later turn out not to be true.

> A customer stated they had been telephoned by their service provider and offered a 'new deal' without being told they were entering into a further 24-month contract which they would have to pay an exit fee to cancel.

7.48 It is a particular problem when businesses justify a price rise at renewal as due to increased costs, or their assessment of the consumer's risk, when in fact the price is open to negotiation. This practice adversely impacts those

[227] The CPRs bans misleading actions and omissions. The FCA's principle for businesses 7 requires firms to have regard to customer information needs and to ensure that all communications are clear, fair and not misleading and there are specific rules in insurance (ICOBS 2.2.2R) and retail banking (BCOBS 2.2.1R) that mirror this principle. Ofcom general condition C1 sets out minimum terms and information that must be included in broadband and mobile contracts in a 'clear, comprehensive and easily accessible form'. This information includes, among others, the minimum service quality levels, details of prices and tariffs, duration of the contract and conditions for cancellation.
[228] Such statements are problematic when used in advertising to attract new customers, too, since these also mislead existing customers planning to renew. For an example of such a misleading statement see ASA, *Ruling on Vodafone Ltd*, 10 October 2018.

consumers who assume that the renewal quote is the best the supplier will offer or are unable to negotiate. The latter is likely to include vulnerable consumers. It is also not in consumers' best interests to have to engage in time consuming or pressured negotiations.

Failing to give information that consumers need

7.49 It is also a problem when businesses fail to give information that consumers need. We have come across examples of consumers finding it hard to discover what other products their supplier offers, which might be more suitable for them. Other information that customers need, especially at renewal, relates to how much they have been paying for the product and how they have been using it (such as how much data they use per month). We consider how information on usage can assist customers in switching in chapter 6.

Giving information too late or in a format that is not useful

7.50 Consumers can struggle to process information effectively when they feel overloaded or are placed under time pressure. In one complaint we saw, a car insurance customer was offered a number of different products over the telephone, with subtle variations in price and cover. He felt unable to fully evaluate the choices over the phone as he felt under pressure from the agent and the upcoming renewal date.

7.51 This can be a particular problem for vulnerable consumers who have poor digital skills or limited internet access and may miss important information.

> One customer complained that his elderly father (83) had been offered 'free' telecoms equipment instore but did not realise he would be charged at the end of the contract. The information about the bill and the package had been emailed to an address the customer did not use and did not know how to access, resulting in the customer unknowingly paying for five years.

Stopping the practice of making it hard to access information

7.52 Information given to consumers needs to be truthful, comprehensive and accessible. It must not be misleading. Businesses should provide consumers with the information they need to make informed decisions and ensure customers can access important information. For example, suppliers should ensure they have up to date contact details, and communicate clearly in a way that enables individuals, including the vulnerable, to access and understand it.

What can be done to stop these harmful practices?

7.53 The practices outlined in this chapter are harmful to consumers and are unacceptable. They have serious consequences for consumers, especially the vulnerable, and in some cases are a deliberate attempt by businesses to take advantage of customers. These practices also impose a cost on the economy, both in terms of the amount of time consumers have to spend negotiating or switching to get a better deal, and because those who do not negotiate or switch can end up paying far more than others.

7.54 There are laws and rules which apply to this area. Businesses that engage in these practices may face enforcement action - whether by the CMA, Trading Standards or the relevant regulator, who can use their powers to enforce consumer law as well as under their sector-specific rules.

7.55 In Annex F we describe these relevant laws, and Ofcom and the FCA's regulatory powers in further detail. This includes relevant examples of enforcement action and other areas of work which they have been undertaking using their sector-specific powers.

7.56 Both Ofcom and the FCA have taken enforcement action to tackle the harmful business practices that we have discussed earlier in this chapter, in their regulated markets. For example:

a) Ofcom has an ongoing enforcement programme looking at exit fees in its sectors, in particular to ensure that these fees are not excessive and are fair and transparent. It recently issued fines against Virgin Media and EE for charging excessive exit fees;[229] and

b) the FCA has taken action for example a fine against Homeserve Membership Ltd of £30.6 million for mis-selling of home emergency and repairs insurance cover and providing inadequate information to customers.[230]

7.57 Our illustrative evidence of such practices covers markets across the economy. While this is not an in-depth review, it nevertheless shows that there is more to do to protect consumers. There must be a concerted effort by

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[229] Ofcom, *Enforcement programme into early termination charges*, June 2018, Ofcom, *Investigation into Virgin Media's early termination charges*, November 2018; Ofcom, *Investigation into EE's early termination charges*, November 2018.
[230] FCA *Final Notice to HomeServe Membership Ltd,* 12 February 2014.

the CMA and regulators to identify and stop these harmful practices across different markets. Here we briefly consider the existing general legal framework across markets to enable this.

Current consumer law applicable across markets

7.58 Consumer law in the UK is primarily principles-based and applies to all markets, including the five markets identified in the super-complaint. It stipulates a number of practices and contract terms that should not be used by businesses against consumers. We have set out further detail about the specific laws in this area in Annex F and include a brief summary here.

7.59 Suppliers have to provide their services with reasonable care and skill, and in accordance with any statements they make to consumers.[231] This includes where they are taking steps to renew contracts or organise switching.

7.60 Terms in contracts or notices used by suppliers must be fair and properly transparent.[232] This includes terms governing renewal of contracts, changes to the price, and where a supplier may try to exclude liability for statements made by their sales staff during negotiations. Terms that are unfair are not binding on the consumer, and it can be a criminal offence for a supplier to try to rely on them. For example, it could be unfair if a contract term required the consumer to give excessive notice or to follow an onerous process to prevent the contract being renewed against their will, if they are locked into an excessively long contract, or if the supplier could arbitrarily change the price.

7.61 To enable consumers to take properly informed decisions about products, supplier's practices or statements cannot be misleading or aggressive, and they must exercise professional diligence.[233] Telling a consumer their renewal rate is a 'great deal' when the supplier offers cheaper deals could be a misleading action under these regulations. If a company fails to answer calls within a reasonable time, this may be an aggressive practice on the basis that it is a non-contractual barrier to consumers exercising their contractual rights, particularly if a call centre is the only method of cancellation.

7.62 Where a supplier signs up customers on the internet, over the phone, through doorstep selling or by stopping them in the street, they have to provide specific pre-contract information. Consumers also have 14 days in which to change their minds and exit the contract without penalty where they have

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231 Part 1 of the CRA, sections 48-60.
232 Part 2 of the CRA. There are limited exemptions to this rule. See CMA guidance on unfair contract terms (CMA37).
233 CPRs. See also OFT, *Consumer protection from unfair trading: guidance on the UK regulations*, May 2008.

entered into a contract via the internet, telephone or post.[234] These rules require suppliers to be very clear about the price that has to be paid, and they outlaw consumers being signed up to additional products without their agreement (for example where a contract is set to auto-renew by means of a pre-ticked box).

7.63 We have the power to enforce consumer law and engage with a business in order to stop, or to prevent, infringements of consumer law and ensure they are not repeated. In certain circumstances, we can use 'enhanced consumer measures' such as requiring the business to pay compensation in cases where consumers have suffered loss. Regulators have the power to impose fines in relation to breaches of their own rules, and to amend those rules where appropriate (see Annex F).

7.64 While we have the power to prosecute businesses in appropriate circumstances, we do not have a similar power to seek fines under consumer law. Fining powers would improve deterrence and better align our competition and consumer enforcement work.[235]

7.65 Principles-based consumer law is often open to some interpretation, and there can be different views taken as to whether a practice causes harm and is therefore unlawful. Ultimately only a court can rule on whether a term or practice is unlawful. Therefore, we will be doing further work to identify if there are areas of harm related to the loyalty penalty that cannot be addressed fully by existing law or regulations. This may result in legislative and/or regulatory changes to ensure these harmful practices are stopped.

Conclusion

7.66 There are a range of business practices that obstruct and hinder consumers from switching and negotiating in markets. These are particularly harmful in auto-renewal, roll over or subscription-based products and services, which are a common feature of many markets today. These practices enable businesses to exploit customer inertia and charge higher prices for existing customers who struggle to shop around or switch.

[234] Consumer Contract (Information, Cancellation and Additional Charges) Regulations 2013. There are limited exceptions to these rules. Where a company supplies financial services, the Financial Services (Distance Marketing) Regulations 2004 apply.
[235] Either as part of the Part 8 process or under an administrative fining system. For further detail, see CMA, *Modernising consumer markets green paper: CMA response to government consultation*, 17 July 2018.

7.67 We have identified a number of principles businesses should follow in order to avoid causing harm to consumers and infringing the law as it currently applies. We will be undertaking further work to develop these.

- To address the harmful practices around auto-renewals and roll overs:

    - suppliers should provide their customers with an easy to find and use function to stop the roll over or renewal at any time;
    - consumers should be aware and properly notified that the contract will renew, and the terms of the renewal should be notified in good time for them to take action;
    - any changes to the price or the product or service should generally not be made without the consumer's express agreement, either based on clear information in the original contract, or a new agreement at the time of the renewal;
    - auto-renewal onto a fresh fixed term should generally not be used and only where it is clearly and demonstrably in the customer's interests; and
    - after the renewal has taken place, consumers should be given a cancellation right and have an easy means to exercise it.

- To address the problem of lack of choice customers have in auto-renewal or roll over contracts:

    - any auto renewal must be properly agreed to; and
    - consumers should (in most markets) be presented with a clear and prominent (and no less convenient) option to take the contract without auto-renewal and businesses should not put pressure on them to agree to auto-renewal.

- To address the problems experienced in exiting or cancelling a contract:

    - it should be at least as easy to exit a contract as it was to sign up;
    - exit fees should not be used after any initial minimum term, during any cancellation period, or in any situation where the supplier themselves is not providing the standard of service that they have agreed; and
    - any initial minimum term should be restrained and no longer than is strictly necessary to reflect any price advantage the consumer has received, or to allow the supplier to recover expenses they have paid out to provide the product.

- To address the problem of making it harder for consumers to access information:

  - all information suppliers provide to customers should be truthful and not misleading as stipulated clearly under current consumer law;
  - businesses should provide consumers with the information they need about product availability and usage to make properly informed decisions, rather than making this hard to find or access; and
  - suppliers should ensure their customers can access important information, for example by ensuring they have up to date contact details. They should communicate clearly in a way that enables individuals, including those who are vulnerable, to access and understand key information.

7.68 Enforcement of existing consumer law can go a long way towards achieving these recommendations. The CMA has opened enforcement cases and this will be the first step in a wider programme of enforcement work in this area.

7.69 Much of general consumer law is principles-based and therefore sufficiently flexible to tackle these types of business practices. However, this also allows for different views of what constitutes breaches of law and causes harm. Ultimately, this is decided by the courts. Therefore, we will also look at whether changes are needed to law and/or regulations to ensure there is sufficient clarity and that these practices are stopped.

8. Regulating prices

- Pricing interventions are a direct way to address harm arising from the loyalty penalty. They can limit price differences (for example by restricting price walking or price jumps) or restrict the overall level of prices (for example through absolute caps).
- There has been some reluctance to use pricing interventions in the past given that they can have unintended consequences, potentially undermining investment and innovation. They have therefore only been considered in limited circumstances.
- However, while providing active help for consumers and tackling harmful business practices can bring benefits to many, some people still struggle and end up paying much higher prices.
- In these situations, there is a strong case for regulators to consider targeted pricing interventions to protect these consumers, particularly if vulnerable.
- We welcome the further work that Ofcom and the FCA are undertaking in the five markets and make a number of recommendations about possible pricing interventions for them to consider as part of their ongoing work.

Introduction

8.1 In this chapter we review various remedies that regulate prices. The chapter is structured as follows:

a) the general approach and background to regulating prices;

b) a summary of the different types of potential pricing interventions to address the loyalty penalty and how they could be targeted;

c) the applicability of pricing interventions to the five markets; and

d) recommendations on pricing interventions to consider in the five markets.

Approach to regulating prices

8.2 Pricing intervention remedies control the prices that businesses offer and therefore can directly control harmful pricing practices. This is why they are an attractive option to consider when looking to tackle the loyalty penalty.

8.3 Pricing regulation has historically been used to control the prices of monopoly suppliers, such as networks in energy, telecoms and water. These suppliers face no competitive pressures and could charge high prices in the absence of pricing regulation. In retail markets with several competing suppliers, however, pricing interventions have typically been used sparingly and only where there have been major problems with competition and overall consumer harm has been significant.[236]

8.4 This is because regulating prices can have some challenges. It can be complicated to determine and can have unintended consequences, such as leading to price increases for some consumers and negatively affecting innovation, quality and new entry in a market.

8.5 For these reasons, when faced with concerns such as longstanding customers paying higher prices, the CMA and regulators have largely used ‘enabling’ measures. These seek to open up markets and remove obstacles to competition, such as those described in chapter 6, and therefore enhance the competitive process.

8.6 However, in some cases these measures may not help all consumers, particularly the vulnerable. Therefore, engagement remedies may not always be sufficient in tackling the loyalty penalty and preventing its harmful effects. As described in chapter 4, it has become evident that in some markets although there may be fierce competition for new customers, there are other longstanding customers who are losing out by paying much higher prices or staying on much poorer legacy deals. These consumers can end up paying a loyalty penalty, despite competition working well to keep prices low for others.

8.7 Remedies which enable greater engagement and strengthen competitive pressures on businesses in the market continue to be necessary and beneficial. These ensure that businesses continue to work hard to attract and keep customers. In addition, targeted pricing regulations could be used to protect those who are not being reached by these measures and are therefore continuing to lose out.[237] This would also retain the benefits of active competition elsewhere.

8.8 Targeted pricing regulations could focus either on certain products or protecting particular groups of consumers, such as those who are unable or find it very difficult to switch, those who end up paying significantly higher

[236] The energy market provides recent examples of such interventions, with the CMA introducing a cap on the prices paid by prepayment customers due to substantial supply side problems that undermined competition, and government introducing a broader price cap on all SVTs to address the loyalty penalty in energy. Further information is available on Ofgem’s webpages on the prepayment energy price cap and default price tariff cap.
[237] See paragraphs 8.27 to 8.34.

prices and those who are vulnerable. As they are targeted, the risk of unintended consequences can also be significantly reduced.

Summary of approaches to regulate prices

8.9 In this section we consider two main ways to regulate prices in order to reduce the harm to some consumers from the loyalty penalty:

(a) limiting price differences: controlling the relative prices faced by individual customers relative to prices charged to other customers by the same supplier, or controlling the permissible change over time in prices paid by a particular customer; and

(b) absolute price caps: controlling prices through setting an overall maximum price (not relative to other prices), for example based on costs or affordability.

8.10 Both of these approaches can be implemented either on the basis of prescriptive rules (ie detailed formulae that prescribe maximum price levels) or on the basis of broader regulatory principles (for example that price increases must be justified by increases in costs).

Limiting price differences

8.11 Limiting price differences would directly constrain the ability of suppliers to charge higher prices to longstanding customers than to new customers. These approaches address the harm arising from the loyalty penalty by limiting the overall size of the price difference.

8.12 We review four main ways to limit price differences, which reflect different forms of a loyalty penalty:

(a) restricting price walking: limiting how an individual customer's price is permitted to increase after the initial discount period;

(b) limiting the spread of legacy deals: restricting price differences across groups of longstanding customers who are on otherwise directly comparable contract terms (or banning these price differences which would, in effect, introduce a single default tariff);[238]

[238] Removing the price difference between these customers in markets where the range of services purchased is relatively narrow will have the same effect as bringing in a default tariff, as there would only be one tariff for customers purchasing the same products and services. An example of this is the option which the FCA is considering of introducing a Basic Savings Rate for cash savings after an account has been open for a period of time (see from paragraph 8.52).

(c) limiting price jumps: restricting one-off increases in price such as the difference between introductory prices and later prices across customers; and

(d) requiring suppliers to move customers to their best available deal: so that longstanding customers are charged the same price as newer customers purchasing the same product.

8.13 Limiting price differences is potentially an attractive option for two reasons. First, it directly addresses the key concern arising from the loyalty penalty, namely that longstanding customers pay much higher prices than new customers. Second, it does not require detailed information about costs to implement.

8.14 However, such pricing interventions can have unintended consequences. For example, there may be a risk of waterbed effects, whereby reducing prices for longstanding customers (and businesses' profits) may reduce the incentive and ability for businesses to offer low upfront prices to attract consumers. As a result, upfront prices to new customers may rise, and the overall strength of competition may be weakened.

8.15 Linking prices together through restricting the difference between them, can also cause a 'tying effect'. This is where suppliers may have weaker incentives to cut prices to attract or retain customers, because if they do so they will also be required to cut prices for other customers. This is likely to be of particular concern where a price control applies across a wide group of customers.

8.16 Further, if one of these price controls is applied to address a particular form of loyalty penalty, suppliers may seek to follow a different approach while maintaining higher prices for longstanding customers. For example, if price walking were banned, suppliers might move towards a price jump model.

8.17 There are also practical challenges in designing and applying these interventions in some markets. For example, in some markets different customers present different levels of risk (as in insurance and mortgages) or buy genuinely different products (as in mobile and broadband where products vary in quality and in the components included in the bundle purchased). These challenges could make it particularly difficult in these markets, for example, for a regulator to set a monetary or percentage limit on price differences between specific customer groups.

8.18 Reflecting these challenges, regulations to limit price differences have rarely been used in recent times. In the energy market, limits on price differentiation which applied in the retail market were assessed to have coincided with a decline in switching rates and evidence of weakening competition over the SVT,[239] and an absolute price cap on SVTs is subsequently being implemented.[240]

8.19 We recognise there are risks and challenges in regulating price differences, which are important to consider in designing effective interventions. However, these are not insurmountable. Where the case for intervention is strong, they can be mitigated through the design of the remedy and in particular by:

(a) targeting the intervention so that the customer group being protected is smaller. This means that businesses are less likely to increase the prices paid by other customers by a significant amount. More generally, any intervention which is targeted at a smaller group of customers is less likely to have an unintended adverse effect on competition across the market;

(b) allowing sufficient flexibility or 'headroom' within the pricing rules, to mitigate the risk that any pricing regulation does not properly reflect the costs to service different customers. This could also include the flexibility to maintain true introductory offers which promote switching and support the benefits of competition; and

(c) where feasible, applying the price controls using regulatory principles which describe unfair pricing approaches, rather than prescriptive formulae. This type of approach could be effective in regulated markets where there is normally extensive data and regulatory reporting to demonstrate compliance.[241]

Absolute price caps

8.20 Absolute price caps seek to directly limit the adverse outcomes of the loyalty penalty by setting a maximum permitted price. A price cap is set relative to an external measure rather than relative to prices that the same supplier offers to other customers. Remedies of this type can vary in respect of:

- the scope of the price cap: whether it applies to all customers or a targeted subset of customers such as those who may be vulnerable or particularly longstanding; and

[239] CMA, *Energy market investigation: final report,* June 2016. The rule banning regional price discrimination was introduced in 2009 and lapsed in July 2012 and was not reinstated. See Ofgem, *Decision on Standard Condition 25A in the gas and electricity supply,* October 2012.
[240] See Ofgem webpages on the default price tariff cap.
[241] Under this approach, compliance would normally be demonstrated ex post through monitoring and reporting. Suppliers could be still at risk of paying fines or have to pay redress to customers in the event that a breach of the rules is identified by the regulator.

- the level of the price cap: which in turn affects the proportion of customers for whom the cap is likely to be binding. If the cap includes significant 'headroom' above predicted costs of providing the service, it becomes a 'safeguard' cap that limits only the very highest prices.

8.21 An absolute price cap is most likely to be practicable where there are relatively homogenous products, readily available information on costs and where the tariffs offered by suppliers differ as to price (or per unit price) but with a broadly similar level of service and otherwise comparable terms and conditions. Under these circumstances, absolute price caps have the benefit over limiting price differences in that they do not cause a tying effect (described in paragraph 8.15). They are however more challenging to implement where there are larger variations in products, such as quality and other elements (for example risk in insurance, data or speed in telecoms).

8.22 Price caps have typically been set where there is either a monopoly or a business with a dominant position, described as significant market power (SMP) in telecoms. For example, regulation applies to the wholesale charges made to retail broadband providers by the network operator, Openreach, which has SMP. Ofcom consulted on proposals to regulate BT's standalone landline tariffs, as it identified that BT had SMP for customers on this tariff.[242]

8.23 A price cap is also being implemented for all retail energy customers on a SVT, by means of the Domestic Gas and Electricity (Tariff Cap) Act 2018.[243] The FCA and Ofcom have also imposed price caps where they have identified specific risks of harm to customers in the relevant markets.

8.24 For example, the FCA has applied price caps in respect of high cost, short term credit (payday loans)[244] and is consulting on proposed rules that would apply a price cap to rent-to-buy agreements.[245] Ofcom has recently imposed a price cap on 118 directory enquiries numbers.[246] These price caps have been introduced to limit harm and protect consumers, in particular vulnerable consumers, which we support.

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[242] Ofcom consulted on its findings that BT had SMP in this market, but then subsequently accepted a voluntary offer from BT to reduce these tariffs. See Ofcom, *Review of the market for standalone landline telephone services,* February 2017.

[243] Domestic Gas and Electricity (Tariff Cap) Act 2018. While there are many energy suppliers, the CMA found in its energy market investigation that these suppliers were able to exert market power over their less active customers, resulting in higher prices for them. See CMA, *Energy market investigation: final report,* June 2016.

[244] FCA, *Detailed rules for the price cap on high-cost short-term credit Including feedback on CP14/10 and final rules,* November 2014.

[245] FCA, *Rent-to-own and alternatives to high-cost credit – feedback on CP18/12 and consultation on a price cap,* November 2018.

[246] Ofcom, *Directory enquiries (118) review: statement,* November 2018.

8.25 However, absolute price caps, particularly where applied across a large group of customers, raise some design challenges. Unlike limitations on price differentiation, absolute price caps explicitly constrain suppliers' ability to recover total costs from at least some customers and therefore risk undermining the financial stability of the market. There are also other risks associated with absolute price caps, which include setting the cap too low (either due to error in design or changes in costs), providing a focal point where suppliers price up to the cap and the waterbed effect described in paragraph 8.14).

8.26 These can be minimised by directly targeting the cap at specific customer groups or tariff types. For example, the cap on gas and electricity prepayment meter tariffs (the PPM cap) introduced by the CMA in its energy market investigation.[247] A further example is in the postal market, where Ofcom applies a safeguard cap to second class standard letters, to ensure an affordable universal service product is available to all.[248]

How to target pricing regulations

8.27 The targeting of pricing regulations (whether the control limits price differences or imposes an absolute price cap) can be a way to realise their benefits while mitigating the risks of unintended consequences. In this section, we consider how measures can be targeted to groups of consumers and some practical questions about how this can be achieved.

8.28 In some cases, it may be more straightforward to identify the groups targeted for protection, such as those on poor value legacy deals, those who have stayed with their supplier over a certain period of time, those unable to switch or those paying much higher prices than others. However, there may be some challenges in identifying consumers who are more at risk or may be vulnerable.

8.29 One way of addressing this is to use supplier's data on their customers to identify those who may have characteristics associated with vulnerability (see chapters 3 and 4). However, suppliers may not necessarily collect this data, and there may be inconsistencies of approach or definitions. This also

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[247] See Ofgem's webpages on the prepayment energy price cap. In Ofgem's initial assessment of the impact of this protection, it reported that over 90% of PPM customers were on tariffs priced at or close to the cap and there were still opportunities to switch to cheaper tariffs. However, PPM customers' engagement with the energy market remained below average and Ofgem noted that information directly provided by the six large suppliers suggests that there have been lower churn rates following the implementation of the safeguard tariff. See Ofgem, *State of the energy market 2018 report,* October 2018, pp 32-37.
[248] Ofcom imposes safeguard caps on second class standard letters, large letters and packets up to 2kg (see Ofcom, *Securing the Universal Postal Service,* March 2012). The current caps are set to expire on 31 March 2019 and Ofcom has consulted on the level and scope of the safeguard caps to be imposed from 1 April 2019 (see Ofcom, *Review of the second class safeguard caps 2019,* July 2018).

requires customers to self-identify as vulnerable, which they may not wish to do. Therefore, this approach could have practical limitations and vary between markets.

8.30 Existing examples of interventions targeted at vulnerable consumers include Ofgem's price cap for consumers who receive the Warm Home Discount (WHD),[249] and BT's social tariff, BT Basic.[250] The eligibility criteria for both schemes are based on Department for Work and Pensions benefits data. Under the WHD, suppliers also provide the discount to customers they deem in or at risk of fuel poverty (subject to criteria and guidelines) and that apply for it, or that suppliers have identified as potentially vulnerable.[251]

8.31 In comparison to the WHD, take up of the BT Basic social tariff in telecoms is relatively low, although the potential reach of the tariff is higher.[252] Ofcom has noted this may be due to low awareness – eligible customers are not automatically placed on the tariff. It may also be that the bundle of services does not meet customer needs.[253] The BT Basic landline-only tariff, which is provided by BT in its role as a universal service provider (USP), originally had over 600,000 customers following an initiative by Ofcom to encourage BT to identify eligible customers.[254] This had fallen to around 300,000 by 2016. In 2014, BT introduced a voluntary add on BT Basic bundle including broadband, but take up of this service has been very low.

8.32 We consider that measures which require suppliers to offer cheaper tariffs to vulnerable consumers will be more effective where those tariffs can be designed to meet customers' needs, and where there are sufficient incentives or requirements on providers to encourage customers to switch to these tariffs. In addition, it would be necessary to ensure that, where particular categories of consumers are targeted through a price control, these same consumers are not discriminated against by suppliers in terms of the availability of introductory offers.

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[249] The Warm Home Discount Scheme is targeted at the fuel-poor, and offers £140 discount to qualifying customers of participating suppliers. Fuel-poor pensioners receiving Pension Credit Guarantee Credit are eligible and most are identified by the suppliers through a data matching exercise and so receive the discount automatically. These customers also need to be on a SVT or default tariff. Government has stated in its consultation response on the 2018/19 scheme that the WHD benefits two million households.
[250] As described on BT's website.
[251] This refers to the 'broader group' element of the Warm Home Discount scheme.
[252] Ofcom's analysis of BT Basic take up is included in its Access and inclusion report, 2016. Ofcom estimated that over four million customers would be eligible for BT Basic. KCOM also offers a social tariff in the Hull area where it is the universal service provider.
[253] The BT Basic bundle including broadband offers 15GB per month, and was designed to be a light user tariff.
[254] BT Basic was introduced following Ofcom's review of the universal service obligation in 2006. Ofcom determined that BT could withdraw a previous low user tariff only if it identified 600,000 customers for its new social tariff. See Ofcom, *Review of the universal service obligation,* March 2006, page 11.

8.33 There may be further ways to improve the ability of suppliers to identify and help vulnerable consumers. Recent work by Ofwat and Ofgem through the UKRN is an interesting example of what may be possible through data sharing. The UKRN has been supporting the launch of a pilot vulnerability data sharing programme in the North West.[255] In November 2018, UKRN published a progress report that showed that, while there were practical challenges, there had been significant progress towards cross-sector data sharing.[256] This demonstrates the potential for identifying vulnerable consumers for targeted interventions.

8.34 There remain a number of challenges and we encourage regulators and government to continue to consider ways to more effectively identify groups of vulnerable consumers in markets where targeted pricing interventions or protections would be beneficial. The most effective way to target remedies may vary across markets. Nonetheless we welcome and encourage ongoing efforts to investigate what more can be done in this regard.

Which approach to use

8.35 The most appropriate form of any pricing intervention will vary across different markets. In determining this, a range of factors need to be taken into account, including the following:

(a) the form of the loyalty penalty. We have identified a number of ways to limit price differences, which can be targeted at the particular pricing practices observed in the markets where the regulator has concerns;

(b) the proportion of customers to be protected. If, as in energy, a very broad range of customers must be protected, then an absolute price cap may be more effective at lowering prices than limiting price differences;

(c) the characteristics of the product. Absolute price caps can be applied in markets where products are relatively homogenous, such as energy, or where there is a core product, such as Ofcom's proposed safeguard cap in broadband,[257] and where robust information on costs is readily available. Where these conditions do not hold, controls on price differences may be the only available option;

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[255] The pilot aims to make better use of water and energy supplier customer data with a view to identifying customers in vulnerable situations, thereby creating a joint priority services register to avoid vulnerable consumers having to register on multiple occasions with different suppliers.
[256] UKRN, *Making better use of data to identify customers in vulnerable situations: a follow up report*, November 2018.
[257] Ofcom, *Delivering the broadband universal service,* December 2018.

(d) the ability to identify and separate a group of customers which should be protected. In some markets, there may be a clear relationship between vulnerability and higher priced tariffs. In others, some vulnerable customers might also be paying lower prices, and so might pay more as a result of an intervention which reduces the gap between the most expensive and cheapest tariffs; and

(e) the stringency of the control to be imposed. Any intervention will require a detailed assessment of the trade-off between increasing effectiveness by imposing a tighter or more universal intervention and reducing the risk of unintended consequences, by targeting the intervention or setting it in a way that gives suppliers greater flexibility to charge higher prices.

8.36 The most appropriate intervention in any individual case will therefore depend on a number of different factors. Any of the forms of price control described here will have both benefits and risks of unintended consequences. The appropriate form of intervention will be one which is best able to achieve the benefits of reducing consumer harm, while mitigating these risks.

Conclusion

8.37 There are a number of different types of pricing interventions that could directly address the harm arising from the loyalty penalty. They can either limit price differences between customers, limit prices changes (for example by restricting price walking or price jumps) or restrict the overall level of prices (for example through absolute caps). The appropriate choice between these approaches will depend on a number of factors, including the form the loyalty penalty takes, the proportion of customers to be protected and the characteristics of the product.

8.38 There is a strong case for regulators to give greater consideration to targeted pricing interventions to protect particular groups of consumers from the effects of a loyalty penalty. These could include:

(a) customers who are unable to switch;

(b) longstanding customers who do not switch for a number of years and end up paying much higher prices; or

(c) groups of vulnerable consumers which can be identified by the regulator or by suppliers, and which are on relatively expensive tariffs.

8.39 Pricing interventions may have distortionary effects, but these are likely to be more limited when they are targeted to an identifiable customer group subject to the greatest financial harm. We recommend that regulators consider the potential benefits of such targeted pricing interventions when assessing markets more generally, and in particular as part of the ongoing work in the five markets, as discussed in the next section.

Applicability to the five markets

8.40 In this section we review the potential for pricing interventions in the five markets and highlight the potential interventions which we recommend the regulators consider further. These would need careful consideration by regulators to weigh up the risks and benefits to different consumers.

8.41 In some areas, where the pricing practice is unfair as a matter of principle or may be considered misleading or unfair as set out in chapter 7, we take a firmer view that an intervention is required. Examples of this are the practice of charging for mobile handsets beyond the minimum term, and opaque price walking practices.

8.42 The FCA and Ofcom currently have certain legal powers to implement pricing regulations if appropriate. Before implementing remedies, they are required to undertake a legal assessment on the basis of their statutory objectives and duties.[258] This would also require the rules to be compliant with the relevant EU legislation.[259] We have not sought to undertake such an assessment, which would in any case depend on a range of factors including the scope, structure and design of any remedies.

Mobile

8.43 As set out in chapter 4 there is evidence that in mobile:

(a) There is a loyalty penalty where customers on bundled contracts including handsets, continue to pay the same price at the end of their minimum term even though, in effect, their handset may have already been paid off.[260] In many cases, these customers are not aware that they have the

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[258] For example, the Communications Act 2003 requires Ofcom to assess whether any regulations imposed through the use of regulatory conditions are proportionate, objectively justified, transparent and do not unduly discriminate. Ofcom also has powers to impose SMP conditions on operators with SMP and has powers to impose USP conditions on the designated USP. Ofcom is consulting on USP conditions in respect of the new broadband universal service obligation, which it proposes to apply to BT and KCOM. Se Ofcom, *Delivering the broadband universal service,* December 2018.
[259] For example, the European Electronic Communications Code. See Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018.
[260] Ofcom's current data suggests that approximately 1.5 million people may be paying more than necessary on their mobile handset contracts and that collectively, UK mobile consumers could be overpaying by around £330 million each year. However, Ofcom is currently collecting further information to arrive at a more precise estimate as it has had some indications that a larger number of consumers may be affected. See Ofcom, *Pricing trends for communications services in the UK,* May 2018, page 22.

option to move to a SIM-only tariff which may provide directly comparable services for a lower price.[261] Ofcom is currently consulting on requirements for communication providers to send annual end of contract notifications to their customers, with information included on the 'best tariff' available to the customer for their service. For bundled handset and mobile customers, best tariff information must include at least one SIM-only deal.[262]

(b) Further detailed evidence collection is necessary to understand whether longstanding SIM-only customers pay a penalty. The existing aggregate data does not suggest that they do, but Ofcom is undertaking further analysis.[263]

8.44 There are currently no pricing regulations in place for retail mobile services. However, as part of Ofcom's consultation on mobile handsets it is consulting on two options. The first is based on improving transparency and the second is based on requiring providers to move bundled handset and airtime contract customers onto a fairer tariff (for example a SIM-only tariff) when their minimum contract period ends. The latter is a form of pricing intervention.[264]

8.45 As a matter of principle, the practice where customers continue to pay a higher combined handset and airtime price after the minimum contract period ends, so the customer has effectively already paid for the handset, is unfair and should be stopped. We therefore support the second option that Ofcom is consulting on, which would introduce fairer tariffs that would apply at the end of a fixed commitment period. We recognise, however, that there are a number of implementation issues and we do not conclude on which of the mechanisms within Ofcom's second option is appropriate.

8.46 We do not consider other possible price caps in the mobile market given that the existing evidence does not appear to show a widespread loyalty penalty outside of bundled handset and airtime contracts. We welcome Ofcom's ongoing work to gain more evidence on the prices paid by different customer groups. If there is evidence that particular groups of vulnerable consumers are paying much higher prices, consideration could be given to introducing a

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[261] See chapter 6 for more details.
[262] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018.
[263] As part of the data gathering exercise on mobile handset contracts, Ofcom is also collecting data on SIM-only prices for further analysis.
[264] Ofcom, *Helping consumers to get better deals in communications markets: mobile handsets*, September 2018.

safeguard tariff for those customers, drawing on similar approaches currently in place in fixed telecoms.[265]

Broadband

8.47 As set out in chapter 4 there is evidence that in broadband, on average, out of contract customers pay more, with average spend increasing with tenure.[266] There are a wide range of prices for broadly similar products and the use of promotional pricing, after which there is a sharp jump in price at the end of the minimum contract period.[267]

8.48 Ofcom has not to date introduced any pricing regulation remedies in the retail broadband market. However, it is currently consulting on a safeguard cap for customers using a universal service obligation broadband service.[268] We welcome Ofcom's recent announcement that it is in the process of reviewing broadband pricing in more detail.[269]

8.49 The evidence suggests there may be some out of contract customers who are paying more than necessary or receiving a more limited package of services than other customers receive for a similar price. If Ofcom's review finds this is a sufficiently large problem, we think Ofcom should consider an intervention which requires providers to identify obsolete or legacy deals offered to customers on monthly rolling contracts, and to move customers onto better tariffs available to other existing customers on otherwise comparable terms (ie other tariffs with no fixed contract period).

8.50 Ofcom's review of pricing practices in fixed broadband will seek to identify the prices paid by vulnerable consumers.[270] If some vulnerable groups are on poor value tariffs, we recommend that Ofcom, as part of its review, consider whether there is a case to impose targeted protection for those customer groups. This would go beyond the voluntary undertakings currently offered by BT, for example, either through an agreement to offer a safeguard cap for a group of identifiable vulnerable customers which is sufficiently flexible to meet

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[265] The basis for BT's social tariff in fixed telecoms is specific to the universal service obligation, and there is no equivalent in mobile. Therefore, the basis for any comparable tariff would need to be different. However, the principle of offering a targeted discounted tariff could apply equally in mobile, which is now used by some consumers on low incomes as an alternative to fixed telecoms.
[266] See Annex C, Figure 6. Although this demonstrates a pattern of higher spend for customers with longer tenure, it is not able to separate out the effect of tariffs from the possibility that different customer groups have different usage patterns.
[267] The impact of discounting is reviewed in chapter 10 of Ofcom's 2018 pricing trends report.
[268] Ofcom, *Delivering the broadband universal service,* December 2018.
[269] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018.
[270] Ofcom, *Helping consumers get better deals: consultation on end-of-contract and annual best tariff notifications, and proposed scope for a review of pricing practices in fixed broadband*, December 2018.

those customers' needs, or through a targeted discount scheme for qualifying customers purchasing relevant tariffs.

Cash savings

8.51 The FCA has identified that interest rates on easy access cash savings products are lower for longstanding customers. The average rates identified by the FCA fell sharply for customer accounts open for more than two years.[271] The FCA has sought views on alternative options to address the financial harm to customers caused by the loyalty penalty and are due to publish the feedback and its next steps in early 2019.[272]

8.52 The FCA indicated in a recent discussion paper that its current preferred intervention in this market is the Basic Savings Rate (BSR) remedy. The BSR would require providers to apply single (default) interest rates, respectively, to all easy access cash savings accounts and to all easy access cash ISAs which have been open for a set period of time (for example, one year). Each provider could decide the level of their BSRs, and would be able to vary them, subject to applicable legal requirements.[273]

8.53 This remedy would essentially prohibit price discrimination within long tenured savings accounts (ie prevent price walking or legacy pricing) but allow differentiation between short and long tenured savings accounts (ie allow introductory pricing). However, this intervention could result in lower interest rates for some groups of consumers as an unintended consequence. As part of assessing the BSR option, the FCA modelled how it could work and the estimated potential impacts.[274] This analysis used an economic model which captures 'the main dynamics of the market and simulates firms' responses'.[275] From this modelling it appears that the benefits to longstanding customers will be greater than the losses to those that may receive lower interest rates as a result.

8.54 We welcome the FCA's further consideration of plans to tackle the loyalty penalty in this market. Although we have not undertaken a detailed review of the BSR, it is an approach that might limit the harmful effects from the loyalty penalty. The proposal might also bring wider additional benefits, relating to transparency in the interest rates that banks set, by lowering search costs for consumers.

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[271] FCA, *Price discrimination in the cash savings market,* July 2018, Figures 2 and 3.
[272] FCA, *Price discrimination in the cash savings market*, July 2018.
[273] FCA, *Price discrimination in the cash savings market*, July 2018, paragraphs 5.1 and 5.2.
[274] FCA, *Price discrimination in the cash savings market,* July 2018.
[275] FCA, *Price discrimination in the cash savings market*, July 2018, paragraph 5.8.

8.55 If the FCA implements the BSR, we recommend it evaluate whether the BSR has had the intended impact and if not, consider further pricing interventions such as a targeted absolute price floor on the savings rate.

Home insurance

8.56 The evidence provided by Citizens' Advice and the FCA shows that in insurance markets, many longstanding customers are paying more than new customers.[276] The FCA's evidence indicates that prices paid can rise to around double the initial price after five years with the same provider,[277] and that the pricing in the first year is often below cost to encourage switching. However, the evidence indicates that the practice of real price increases continues long beyond any introductory period.

8.57 The FCA has recently launched a market study looking at how general insurance firms charge their customers for home and motor insurance.[278] It has said it will consider all potential remedies that may be required to make the market work well for customers. Where it finds that there is harm to customers, remedies could include changes to the way firms price insurance, contractual changes or limits on differences in prices between different groups.[279]

8.58 We support the FCA's work in this area and, as part of its review, we recommend that the FCA assess whether consumer harm associated with price walking should be limited through pricing intervention.

8.59 For example, the FCA could consider the option of applying rules which define regulatory principles on what level of price walking in insurance is fair to customers. This could set principles which insurers are required to comply with when setting renewal prices to existing customers.[280] Therefore, we recommend that the FCA consider a targeted pricing intervention as one of the potential options in its market study and assess the potential costs and benefits of this intervention, as part of any package of remedies.

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[276] This is often although not always as a result of an opt out auto-roll over at the end of each contract period onto new contract terms which are worse than the contract terms prior to the auto-roll over. The auto-roll over increases the price, with no corresponding increase in service.
[277] See Annex D, Figure 1. The FCA analysis illustrates that prices change from approximately 65% of cost to 130% of cost over five years.
[278] FCA, *General insurance pricing practices market study: terms of reference,* October 2018.
[279] FCA, *General insurance pricing practices market study: terms of reference,* October 2018, paragraph 4.15.
[280] Although insurance pricing is personalised and complex, it should be feasible to set rules on what level of price increases is justified for some subgroups of existing longstanding customers. We expect there would be complexity in understanding the potential effects of any pricing intervention, as for example any ban on price walking could lead to a greater use of price jumping. The FCA would need to assess this using the data available from its market study.

8.60 As discussed earlier, any intervention has risks of unintended consequences. For example, there could be adverse distributional consequences. If customers on low incomes benefit from lower prices on average more than higher income customers, any interventions could increase the amount these low income customers pay. Equally there could be risks that insurers are able to 'game' any new rules in terms of how they set prices, and to make the case for continued price walking, justified by increases in costs for certain customer groups.[281]

8.61 The purpose of the FCA's market study is to understand more about how pricing works in practice. This should provide further evidence to determine the nature of the consumer harm, who is affected by it and whether a proportionate remedy can be designed which mitigates these risks. If the FCA's analysis indicates that the harm from the loyalty penalty is sufficiently large to justify further action, we expect that the market study will consider a wide range of remedies designed to limit this. As part of that study we recommend that targeted pricing interventions should also be considered as part of the FCA's overall assessment, alongside other potential remedies.

Mortgages

8.62 In 2016 the FCA launched a market study which found that overall the mortgage market is working well in many respects, but that it could work better in a number of ways, including the fair treatment of customers who do not or cannot switch, ie those impacted by the loyalty penalty.[282] See Annex D for more details.

8.63 There are two harms to longstanding customers that have been identified in mortgages. They are:

(a) that customers who are rolled onto a reversion rate such as a SVR at the end of an introductory deal face a sharp jump in the price paid, with the reversion rate being high relative to the prices that customers could receive from a new introductory deal;[283] and

[281] There are a number of potential ways to mitigate risks of any pricing intervention, including allowing some flexibility for insurers and a sufficient introductory period for new customers before it starts to apply.
[282] FCA, *Mortgages market study: interim report,* May 2018, paragraph 1.12 and from paragraph 1.27.
[283] In the FCA's work, the term 'introductory deal' includes internal transfers ie where customers switch to a new fixed deal with the same provider.

(b) that some of these customers are unable to switch mortgages, due to changes in eligibility criteria, and are therefore unable to access the competitive prices available in the market (mortgage prisoners).[284]

8.64 The FCA is actively looking into how to reduce the harm to customers who are unable to switch, which we support. There has already been progress for customers of active lenders who are unable to switch. Lenders have come to a voluntary agreement, whereby the lender offers an internal switch to customers who are currently unable to switch.[285]

8.65 Some borrowers are with inactive firms which are no longer lending or are part of a mortgage book which has been sold to entities not authorised for mortgage lending. The FCA currently has far fewer options to improve the ability for these consumers to switch compared to customers with active lenders. The FCA has begun discussions on possible solutions for inactive lenders with relevant firms, consumer groups and government.[286]

8.66 In addition, given the scale of the difference between reversion rates and the pricing of introductory deals, we also recommend that the FCA investigate the characteristics of other customers who have been on a reversion rate for long periods of time and the reasons why they stay on the rate. If this work indicates that these customers are vulnerable, the FCA should consider measures to help or protect these customers.

Recommendations

8.67 In this chapter, we considered a range of pricing interventions to tackle the loyalty penalty, and the applicability of these measures to the five markets identified in the super-complaint.

8.68 These measures directly deal with the effects of the loyalty penalty and for that reason are an attractive option. There are risks and potential unintended consequences, however, with any pricing intervention, particularly if these are widely applied.

8.69 We therefore recommend that regulators consider more targeted pricing interventions, for example to protect groups of consumers. This could include

[284] The FCA estimated that approximately 30,000 customers are mortgage prisoners. See FCA, *Mortgages market study: interim report,* May 2018, paragraph 1.29.
[285] FCA, *Statement on the voluntary agreement*, July 2018.
[286] In particular, the FCA is looking at whether it can make any changes to its rules and guidance that could facilitate switching. The FCA will provide an update on this work as part of the final report of its mortgage market study in early 2019.

those who are unable to switch or who find it very difficult and end up paying much higher prices, or vulnerable consumers on higher tariffs.

8.70 In relation to the five markets, in all cases there is work ongoing by the regulators to consider price differences and potential remedies. In some cases, such as cash savings and mortgages, analysis on the extent of the problem and potential interventions is more developed.

8.71 In others, such as mobile, broadband and insurance, the regulators are currently gathering further evidence and undertaking analysis to consider pricing practices and outcomes for consumers in greater detail. This is important to ensure the nature of the problem is sufficiently understood before considering and designing any interventions.

8.72 Where the evidence indicates that there is harm to a group of consumers, and that targeted remedies are feasible and would be expected to achieve better outcomes, we support the regulators in taking forward pricing interventions in these and comparable markets.

8.73 Our recommendations in the five markets are as follows:

(a) in mobile, of the options set out in Ofcom's consultation, we support a requirement on providers to move bundled handset and airtime contract customers onto a fairer tariff (eg a SIM-only tariff) when their minimum contract period ends. It is clearly unfair in principle where suppliers continue to price at the same level after the initial contract when, in effect, the handset has been paid off. This should be stopped;

(b) in broadband, Ofcom is currently gathering information on pricing practices and how they affect consumers. We think that as part of this work Ofcom should consider protections for those that suffer a loyalty penalty, particularly if they are vulnerable. Ofcom should consider whether this could be through a remedy that moves customers on poor value legacy deals onto newer better value deals. We also recommend that Ofcom consider whether pricing interventions such as targeted safeguard caps could be put in place to protect vulnerable consumers more effectively than existing social tariffs;

(c) in home insurance, we welcome the FCA's ongoing work in this market. As part of that work, we recommend that the FCA investigate pricing practices and consider targeted pricing interventions that limit price walking, for example rules to restrict this practice, as part of a package of remedies to address loyalty penalty in this market;

(d) in cash savings, we support plans to tackle the loyalty penalty. If the FCA introduces the BSR or a comparable remedy, we recommend that it subsequently evaluate whether it needs to be strengthened through further pricing interventions such as a targeted absolute price floor, particularly to protect vulnerable groups of consumers; and

(e) in mortgages, we support the FCA's work to help customers who currently cannot switch. We also recommend further work is undertaken to understand the reasons why some customers are staying longer, whether they show vulnerable characteristics, and if so, what if any, further targeted interventions may be necessary.

9. Conclusion, recommendations and next steps

9.1 This chapter summarises our overall conclusions on the issues raised by Citizens Advice, sets out our recommendations for action and the next steps we and others will take following this response.

9.2 We have found that there is likely to be a substantial loyalty penalty paid by consumers each year. Existing estimates suggest this could be around £4 billion across the five markets highlighted by Citizens Advice (mobile, broadband, cash savings, home insurance, mortgages). However, it is also likely to arise in many other markets where services are automatically renewed or rolled over.

9.3 While some very active consumers are getting cheap deals, many others are losing out. Some think that staying 'loyal' will pay off, do not realise they are paying much more or struggle when they try to shop around as it can be difficult, confusing or time consuming. These challenges can be even greater for those who may be vulnerable. This erodes people's trust in markets and many consumers feel let down or frustrated.

9.4 Businesses can make this worse by making it even more difficult or confusing for their existing customers to either change or get better deals. Examples of these practices include imposing continual 'stealth' price increases, not giving customers enough warning before being rolled over or making it more difficult to leave than it is to sign up.

9.5 Tackling these problems head on is overdue. There have been and are continued efforts by regulators and government. But these have not made sufficient progress. In many cases too much has been asked and expected from consumers, and not enough from suppliers. There is a clear case for intervention to protect those who are hardest hit, particularly those who are vulnerable.

9.6 Based on our investigation we consider the best ways to achieve change are:

- providing genuine support to consumers through the use of smart data, intermediaries (PCWs, automatic switching services and local face-to-face advisory services) and collective switching which offers exclusive tailored deals;
- enforcement to tackle harmful and unacceptable business practices; and
- targeted pricing interventions to limit price differences, such as restricting price walking or capping prices for those worse off, in particular vulnerable consumers.

Recommendations

9.7 We are recommending eight key reforms to address the problems related to the loyalty penalty across markets.

A. *Stopping harmful business practices*

1. Bolder use of existing enforcement and regulatory powers to tackle harmful business practices. We are launching investigations in the anti-virus software market. [Recommendation to regulators and action by the CMA].

2. Legislative and/or regulatory change may also be needed to tackle these practices, alongside new powers for the CMA to seek substantial fines where law is breached. [Recommendation to government].

B. *Publicising the loyalty penalty to hold suppliers to account*

3. Publish metrics on the size of the loyalty penalty in key markets and for each supplier, for example in an annual joint loyalty penalty report. [Recommendation to regulators].

C. *Giving people more help in getting better deals*

4. Empower intermediaries to support switching, for example considering giving a greater role to local consumer-facing advisory organisations, such as Citizens Advice, who could do more to support switching for vulnerable consumers. [Recommendation to government].

5. Press ahead with the Smart Data Review and roll this out in those sectors such as telecoms where it has the greatest potential to transform markets. [Recommendation to government and regulators].

6. Capture and share best practice on 'nudge' remedies that have been tested and shown to work or not, so that lessons across markets are learnt. Some remedies (such as requiring suppliers to give last year's price on renewal) could be rolled out across markets and potentially strengthened. [Recommendation to regulators (through the UKCN)].

D. *Protecting customers from harm, particularly vulnerable consumers*

7. Consider targeted pricing regulations - such as limiting price differentials, or price caps - alongside other measures where there is clear harm, particularly to protect vulnerable consumers. We also make a number of

recommendations about potential pricing interventions to be considered as part of ongoing work in the five markets. [Recommendation to regulators and the CMA].

E. *Better understanding the loyalty penalty across markets*

8. Assess the feasibility of matching price data to a recurring large scale UK survey to improve our understanding of who pays the loyalty penalty across markets, and whether vulnerable consumers are particularly adversely affected. [Recommendation to regulators].

Our recommendations in the five markets

9.8 We also make a number of recommendations to the FCA and Ofcom on measures to tackle the loyalty penalty, which should be considered as part of their current work in these markets and any other potential remedies.

Telecoms: mobile (bundled handset and airtime) and broadband

9.9 In mobile, we do not consider that providers should continue to charge customers the same rate once they have effectively paid off their handsets at the end of the minimum contract period. This is unfair and must be stopped, and we welcome Ofcom's recent consultation on this.

- We support a requirement on providers to move customers on bundled handset and airtime contracts onto a fairer tariff when their minimum contract period ends. [Recommendation: Ofcom].
- Low levels of awareness and understanding of SIM-only deals could also be tackled, for example through a targeted campaign to complement Ofcom's proposals on best tariff information. [Recommendation: Ofcom].

9.10 Loyalty penalty problems in the broadband market must be thoroughly investigated and we welcome the review recently launched by Ofcom. As part of its review we recommend that Ofcom:

- Consider a number of possible interventions including tackling broadband legacy pricing and targeted safeguard caps to protect vulnerable consumers. [Recommendation: Ofcom].
- Review the feasibility of collective switching for broadband customers, learning lessons from Ofgem's recent experience. [Recommendation: Ofcom].

9.11 Smart data could also be highly beneficial in telecoms markets, both directly to help consumers engage in markets but also to better empower intermediaries.

- We support pushing forward with implementing smart data through the government's current review. [Recommendation: Ofcom].

- We also recommend Ofcom review how it can create favourable conditions for the development of innovative intermediaries in the mobile and broadband markets. [Recommendation: Ofcom].

Financial services: cash savings, home insurance and mortgages

9.12 In cash savings, the FCA has recognised that interventions to date have had limited impact on addressing the harm to longstanding customers. It is currently considering a 'Basic Savings Rate'. We welcome this further work.

- If implemented, we recommend the FCA evaluate whether the Basic Savings Rate has had the intended impact and if not, consider further pricing interventions such as a targeted absolute price floor in cash savings. [Recommendation: the FCA].

- We also recommend the FCA consider whether collective switching can be applied to the cash savings market. [Recommendation: the FCA].

9.13 In insurance markets, evidence suggests that many longstanding customers are paying more than newer customers, with firms repeatedly increasing prices year on year. Therefore we welcome the FCA's current market study and as part of this study we recommend that the FCA:

- Investigate insurance pricing practices and consider pricing interventions that limit price walking, for example rules to restrict this practice. [Recommendation: the FCA].

- Explore how intermediaries can continue to benefit the home insurance market (for example where semi-smart solutions can improve the existing infrastructure of PCWs). [Recommendation: the FCA].

9.14 In mortgages, the FCA is currently undertaking a market study. As part of that study we understand that the FCA is taking immediate action to help those who cannot switch in this market (mortgage prisoners) move onto better tariffs, where feasible. We strongly support that work.

9.15 But there are still 10% of longstanding customers who could switch and make significant savings, but do not.

- We recommend that the FCA find out more about these mortgage customers and why they are not moving and look at what measures can be taken to help or protect these customers if needed. [Recommendation: the FCA].

Next steps

9.16 We have set out a package of recommendations, both across markets and specifically in relation to the five markets identified by Citizens Advice.

9.17 A number of the market-specific recommendations can be taken forward immediately by regulators through their existing studies or ongoing work in each of these markets. Some of the recommendations require further consideration and oversight by the CMA and others such as government and regulators.

9.18 The CMA will be undertaking further work on the loyalty penalty, working closely alongside regulators, government, business and organisations such as Citizens Advice. This will take forward a number of recommendations, as set out in Table 9.1.

Table 9.1: Taking forward our cross-cutting recommendations

Recommendation	Lead
1. Taking forward enforcement cases on these practices.	CMA/Regulators.
2. Explore legislative and/or regulatory changes to clarify harmful practices and develop principles on these.	CMA/Government.
3. Publish key metrics on the loyalty penalty.	Regulators and CMA; for example through the UKRN – as part of its performance scorecard work.
4. Empower intermediaries; greater role to consumer facing advisory organisations.	Government/consumer organisations.
5. Rolling out smart data.	Government/FCA/ Ofcom/CMA – as part of the Smart Data Review.
6. Capturing best practice on 'nudge' remedies.	CMA/UKCN.
7. Consideration of targeted pricing regulation when assessing markets.	Regulators.
8. Who pays the loyalty penalty across markets: feasibility of matching price data to a UK survey.	CMA and regulators – for example through the UKRN.

9.19 In addition to the cross-cutting market recommendations, we also expect the FCA and Ofcom to take into account our recommendations on the five specific markets, through their current work in these markets which is summarised in Table 9.2.

Table 9.2: Ofcom and the FCA's key work in the five markets

Market	Latest publication	Next steps/timing	Regulator
Mobile	Helping consumers to get better deals in communications markets: mobile handsets (published September 2018)	Findings to be published in summer 2019 and final statement in early 2020.	Ofcom
Broadband	Review into price differentiation (published December 2018)		Ofcom
Insurance	Insurance market study: terms of reference (published October 2018)	Interim report to be published in summer 2019. Final report to be published in December 2019.	FCA
Cash savings	Price discrimination in the cash savings market Discussion Paper (published July 2018)	Consultation Paper in 2019 (if proposals are taken forward).	FCA
Mortgages	Market study: interim report (published May 2018)	Final report -early 2019	FCA

9.20 We will provide an update on progress to the newly established joint government-regulator Consumer Forum, led by the Minister for Consumer Affairs, in six months. An update will also be published on our website. The FCA and Ofcom will also provide an update on their progress in the five markets.

9.21 The Consumer Forum provides an important opportunity for us to work more closely together. We support its development and continued oversight on key consumer issues such as tackling the loyalty penalty across key markets and addressing challenges faced by vulnerable consumers.

9.22 We have considered Citizens Advice's request that we undertake a market study into the loyalty penalty across the five markets. We do not believe this is the right approach at present, given the work we have already done and the project we will be undertaking to take forward our cross-cutting recommendations. In relation to the five markets, our recommendations to regulators can be taken forward now in their ongoing work without the need for a market study. We consider this is the most efficient way to achieve results quickly.

9.23 We will consider whether sufficient progress has been made in taking forward both our cross-cutting recommendations and recommendations in the five markets over the next 12 months. At that stage we will take a view on what next steps are necessary, such as whether a market study is needed. The CMA is committed to continuing to drive this work forward to maintain momentum and ensure changes are achieved.