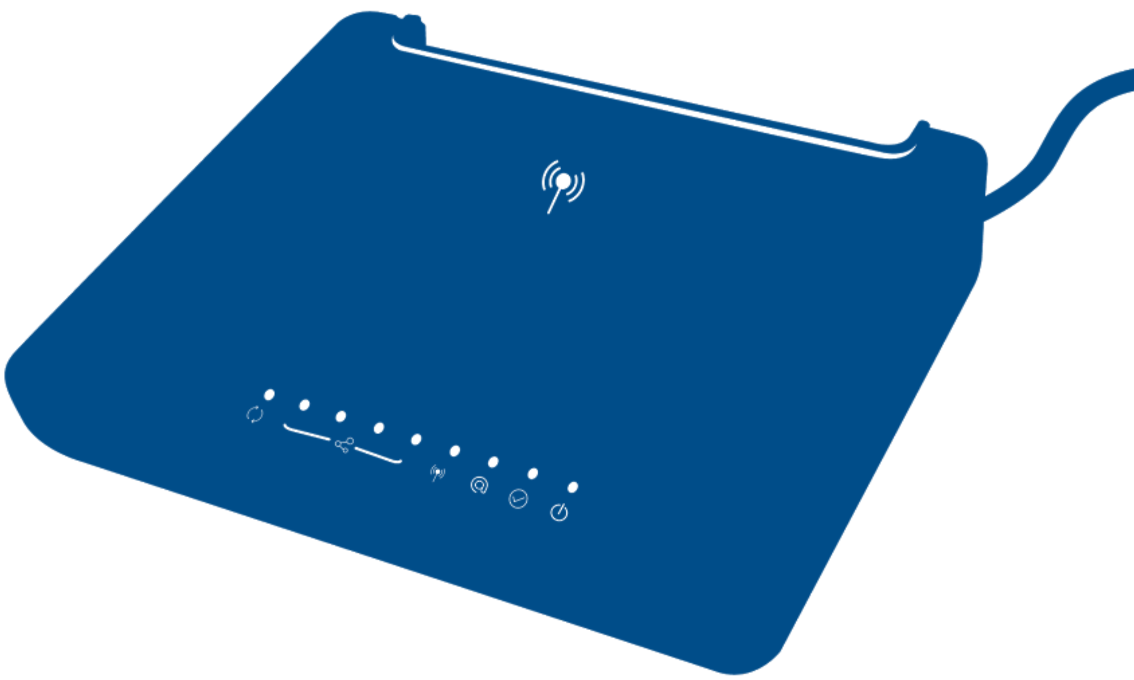
Exploring the loyalty penalty in the broadband market



Roberto Merola and Lizzie Greenhalgh

Contents

Citizens Advice: exploring the loyalty penalty in essential markets

Citizens Advice is currently exploring how customer loyalty is treated across a range of essential markets, including energy, telecoms and financial services. We often think of loyalty as something that should be rewarded but across essential markets we see quite a different response.

This note is part of a series of briefings examining how essential markets exploit consumer loyalty. Providers frequently tempt new customers in with cheaper deals and then raise prices over time, taking advantage of the fact that consumers have busy lives and won't get round to switching until it's too late. As a result, loyal customers often end up on uncompetitive deals, paying far more for a service than a new customer would.

Our new series of briefings on the loyalty penalty urges policymakers to take note. The loyalty penalty is not only unfair because it affects the vulnerable the most, it also suggests that competitive pressures do not apply to significant sections of essential markets.

Summary

Broadband is an essential service for many consumers. 86% of adults in the UK have access to the internet, and many rely on broadband to access key services and to shop for household essentials. However, many broadband customers receive a poor service and then struggle to access compensation.

In 2016, Citizens Advice supported more than 2,000 clients with problems with broadband contracts. In the same year, our Consumer Helpline also handled more than 5,000 complaints about internet service providers. Our data provides us with unique insight into consumer detriment, which our previous research has estimated to be £4.2 billion per year in telecommunication markets. This is the highest of any consumer market.

This policy note focuses on how broadband providers often charge customers a 'loyalty penalty'. Citizens Advice is currently exploring how long-standing customers across essential markets, including energy, insurance, banking and telecoms, are frequently placed on uncompetitive deals, paying far more for a service than a newer customer would. While we typically think of loyalty as a positive trait, our analysis of the cheapest basic broadband deals shows:

- **Broadband customers face an average loyalty penalty of £113 for every year they stay in their contracts after their initial contract period ends, a 43% increase on the initial price**. Proportionally, this penalty is far higher than in other sectors, such as energy, and reflects a recent shift in the market. More than 9 in 10 (96%) consumers think this penalty is unfair.
- **The cost of broadband after the initial contract period is rarely included in advertising and is often hard to locate on providers' websites.** Over a third of customers (35%) say it was not straightforward to find a good deal in essential markets. 35% of customers are unaware of the loyalty penalty.
- **Vulnerable customers are at a greater risk of experiencing the loyalty penalty.** In particular, older and lower income groups are more likely to be loyal. For example, customers aged 65 and over are more than twice as likely than younger customers to have been in the same contract for over 10 years.

This note highlights two opportunities to redress the balance in favour of loyal customers. First, the ASA should require providers to clearly state the cost of broadband after the minimum period alongside the initial price. Price comparison sites should also make it easier to understand this increase. Secondly, Ofcom should monitor consumer detriment and take further action if necessary, such as requiring providers to use smart alerts or introducing price protections for vulnerable customers.

1. Broadband customers can pay a steep penalty for their loyalty

Broadband contracts are made up of an initial period, during which the customer pays the price they have agreed to, and a subsequent out-of-contract period during which the price can change. Our research shows that while initial prices for broadband contracts are shaped by competitive dynamics as providers seek to gain market share, prices for long-standing customers are often much higher as providers take advantage of customer loyalty.

To understand how customer loyalty is treated across the broadband market, this research looks at the cheapest basic broadband tariffs offered online by the 5 providers with the largest market share.[1] Together these providers represent 91% of the broadband market.[2] The analysis compares the price paid by customers during the initial contract period to the tariff they get automatically switched to once the period has ended if they don't renew, cancel, upgrade or switch.[3] While we chose to look at the cheapest basic broadband tariffs for consistency, it is worth noting that these contracts vary in type of broadband, allowed usage and speed. Providers also offer broadband contracts bundled with other additional services (such as TV).[4]

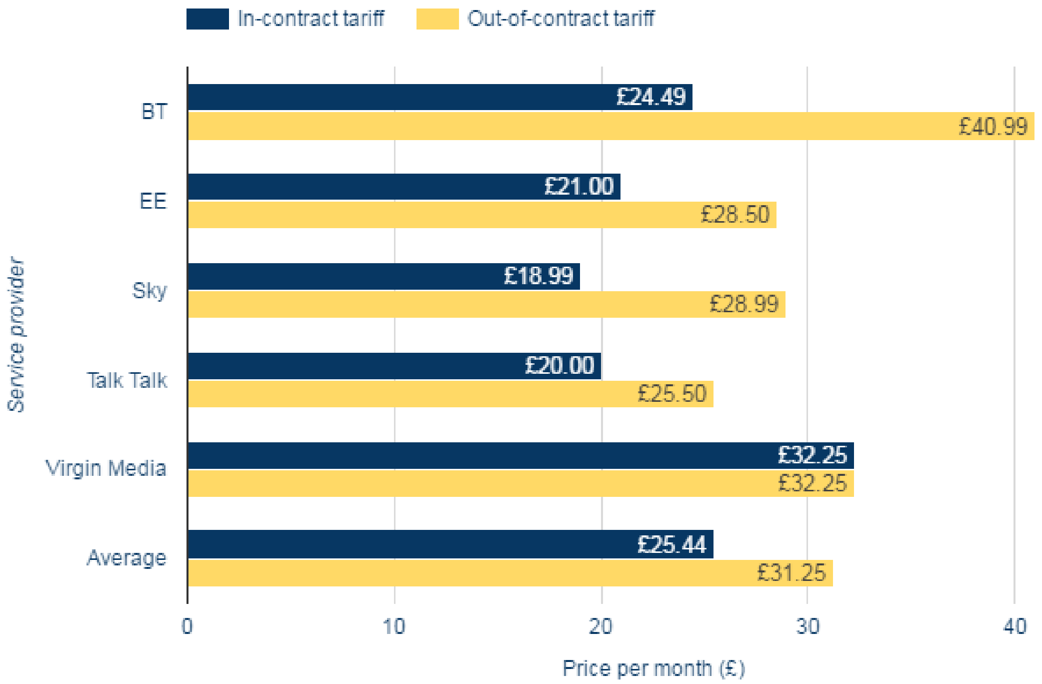
On average, broadband customers on the cheapest basic tariffs with the top 5 providers face a loyalty penalty of £113 per year once they enter the post-contract period. This reflects an average increase of 43% between the initial contract rates and those in the subsequent contract period.[5] This is a much steeper rise than in other markets such as energy, where the average percentage gap is 12%.[6] Customers with BT pay as much as £198 per year, an increase of 67%.[7] Customers on 12 month basic broadband contracts with Virgin Media do not face a loyalty penalty after the initial period, though

---

[1] By basic broadband tariffs we mean broadband contracts with the minimum number of additional services. All providers other than Virgin Media require customers to pay for line rental as part of their basic broadband deals. The Virgin Media basic broadband deal is fibre optic and therefore does not include line rental.
[2] Ofcom, The Communications Market Report, 2016. This is share of residential and SME broadband services. The providers are Virgin Media, EE, BT, Talk Talk and Sky.
[3] This period is 12 months for BT and Sky, 18 months for EE and 24 months for Talk Talk.
[4] While our analysis does not focus on these contracts, 4 out of the 5 largest providers also include loyalty penalties in bundled TV and broadband contracts.
[5] Set up costs were not included in this analysis. See appendix for more detail.
[6] On the basis of data gathered through information requests and Ofgem, we calculated the gap between customers on a standard variable rate and customers on the cheapest available tariff.
[7] BT's tariff was on a time limited offer.

out-of-contract price rises will affect those on bundled contracts.[8] Figure 1 below shows how the loyalty penalty varies from provider to provider.

Figure 1. The cost of broadband rises substantially after the minimum contract period



The loyalty penalty is not uncommon. The majority of broadband customers stay in their contracts after the initial period and therefore pay the increased monthly price. Broadband customers surveyed as part of our research stayed in their contract for almost 4 years on average.[9] By doing so, customers could face a loyalty penalty of as much as £594 over the course of the contract.[10]

43%
average increase on the price of broadband after the initial period

up to **£594**
spent on loyalty by broadband customers over 4 years

[8] These are cheaper than the cheapest 12 month, basic broadband option - see Appendix.
[9] Data provided by Populus. See Appendix for detail.
[10] See the Appendix for the full data table.

2. Broadband customers don't expect their loyalty to be penalised

Many consumers are not aware of the loyalty penalty. 35% of broadband customers surveyed believe that long-standing customers pay the same or less than newer customers. In part, this is because the broadband market is a fast-changing sector, and the rise in monthly costs at the end of the initial contract period is a relatively new problem.[11] Moreover, the prevalence of loyalty schemes in other industries - such as supermarkets and airplane travel - makes it difficult for consumers to understand when they will be rewarded and when they will be penalised.

Furthermore, those customers most likely to pay the loyalty penalty are the least likely to be aware of it. Broadband customers who have had the same contract for more than 3 years are 72% more likely than others to be unsure about how the price paid by long-standing customers compares to that paid by newer customers.[12]

But broadband customers are not just surprised by the loyalty penalty, they also think it is unfair. More than 9 in 10 (96%) believe that long-standing customers should not be charged more than newer customers. In fact, 60% of broadband customers believe that it would be fair for providers to charge loyal customers less than newer customers.

Customers' lack of understanding of the loyalty penalty is also partly due to providers' behaviour. Among broadband customers who have been in their contracts for less than a year, 33% think long-standing customers pay the same or less than newer customers. This research suggest that providers often make it difficult for consumers to assess the true cost of broadband and to choose the most competitive tariff. More than one third (35%) of broadband customers believe that finding a good deal in markets for essential services is not straightforward. In 2016, Citizens Advice supported clients with 2,792 advice issues about finding the best deal in phones, TV, broadband and other markets. This represents a 59% rise compared to the previous year.

---

[11] USwitch, Press release, 9 February 2017. In 2011, after the fixed contract ended consumers paid an average of just £1.84 a month extra for a copper broadband connection and £1.34 a month extra for a fibre broadband connection.
[12] When asked whether they thought that long-standing customers pay more, less or the same as newer customers, 12% of respondents who have been in the same contract for more than 3 years answered 'Don't know', compared 7% of other respondents.

When you look at the way broadband deals are frequently advertised, you can see why so many people experience difficulties navigating them. Previous Citizens Advice research highlighted how many customers were being misled by hidden charges (such as for line rental), resulting in many of them choosing a contract without realising the real long-term costs.[13] Recent regulatory changes now require broadband adverts to include the cost of line rental and to give greater prominence to contract length, post-discount pricing and up-front costs.[14] However, providers are often not being transparent in advertising the cost of their broadband contracts after the initial period.

The table below examines how the main broadband providers display the loyalty penalty on their websites. Virgin Media does not include an automatic out-of-contract tariff rise for its 12 month, basic broadband contract. However, this is only communicated to customers if they use the live chat to speak to a Virgin Media adviser or once they reach the confirmation page. Making it clear for customers that the price of the 12 month, basic broadband contract stays the same after the initial period would make it easier for them to draw comparisons and inform their choices.

How is the loyalty penalty advertised on providers' websites?[15]

Provider	Location	Number of clicks from in-contract tariff	Font size compared to in-contract tariff
BT	Same page as in-contract tariff	0	Smaller
EE	'Buy now' page	4	Smaller
Sky[16]	'Terms & conditions'	2	Smaller
Talk Talk	'Small print'	2	Comparable
Virgin Media	N/A	N/A	N/A

[13] Citizens Advice, Broadband providers 'cashing in on false promises', 22 July 2015.
[14] Advertising Standards Authority, Tougher approach to broadband price claims in ads, 4 May 2016.
[15] We here compare the location of the advertised cost of broadband during the initial contract period to the location of the advertised tariff after the period ends. We counted the number of times a customer has to click on the page to get from the former to the latter. We also compared the font sizes in which the in and out-of-contract tariffs are advertised.
[16] Sky also lists the out-of-contract tariff under the section titled 'Here's the legal bit' (1 click away from the in-contract tariff).

Frequently, broadband providers are no more helpful once consumers enter contracts with them. While most providers voluntarily notify their customers of price increase after the initial contract period,[17] many customers find these prompts unhelpful. Three quarters (75%) of broadband customers say they have never been told by their current provider that they could save money by switching.[18] This is true even for those customers who have been in the same contract for longer than 4 years.[19] However, a large majority (83%) of respondents to our survey think that providers of essential services should inform their customers when they are eligible for a better deal. The high proportion of customers who say they have never been informed about potential savings they could make suggests that existing prompts are ineffective.

Max had a broadband contract for £30 per month. This suddenly jumped to around £100 per month. Because this was paid as a direct debit and the client didn't look at his bill often, he didn't realise this had happened. His provider put him on a higher tariff without informing him that their terms and conditions had changed. He agreed with his provider to be switched to a lower tariff, but this has recently risen. Max again appeared not be informed of the change.

[17] BT, EE and Talk Talk inform their customers via email. Virgin Media calls and emails customers. Sky does not contact customers to remind them their contract is almost up (though it allows customers to keep a tab of the contract duration through their online account).

[18] NB 31% of respondents who say they have never been informed that they could save money by switching have been in their contracts for less than a year. Of the remaining 69% who have never been informed that they could save money by switching, 61% have had the same contract for 3 years or more.

[19] 73% of respondents who have been in their contracts for more than 4 years said they have never been informed.

3. Many consumers don't have time to shop around or switch contracts

Markets should work in a way that reflects consumer behaviour. By understanding the way people navigate essential markets, consumer protections can be more targeted and keep up competitive pressure. Behavioural insights tell us that giving consumers information and encouraging them to switch is not enough to ensure they avoid detriment. Despite recent efforts to drive competition through switching, broadband customers are still likely to stay loyal to their contracts and providers. Over half (51%) of them have been in the same contract for 2 years or more, with 27% in the same contract for more than 5 years. 50% had their previous contract with their current provider.

As our previous research has highlighted, consumers often don't have the time or inclination to shop around in markets for essential services.[20] 2 out of 5 (39%) broadband customers do not want to spend more time shopping around than they currently do, and 28% do not have the capacity to do so. Particularly in markets for essential services, cumbersome processes make customers less likely to engage in decision making.[21]

Customers are even less likely to shop around once they enter a contract. While the majority (63%) of broadband customers try to find good deals before choosing a provider, many of them are unlikely to worry about doing so once they are with a particular company. 71% have done very little or no shopping around since entering their contracts, and 55% have never tried to renegotiate to get a cheaper deal. For many customers, it can be frustrating to regularly check whether the deal they are on is still competitive given the time they spent shopping around in the first instance.

[20] Citizens Advice, Against the Clock, November 2016.
[21] Citizens Advice, Against the Clock, November 2016.

Moreover, loyalty is a habit that is hard to break. Consumers who do little or no shopping around before entering their contract are 54% more likely not to shop around subsequently.[22] Conversely, those who did some or a lot of shopping around initially are almost 5 times as likely than other customers to do the same again.[23]

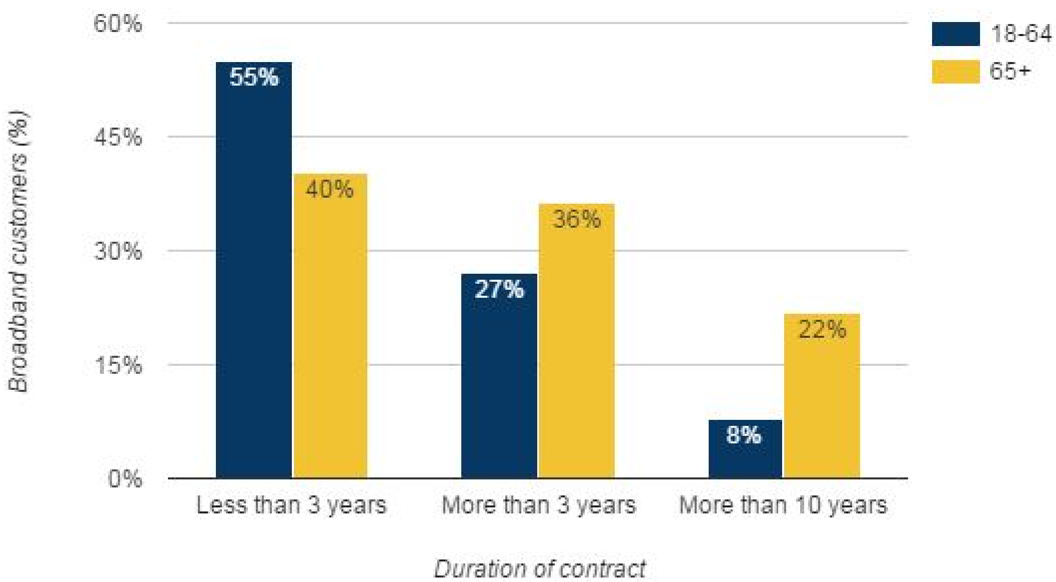
[22] 92% of customers who did very little or no shopping around before entering a contract also did very little or no shopping around subsequently, compared to 60% of customers who did some or a lot of shopping around initially.
[23] 40% of customers who did some or a lot of shopping around before choosing a contract also shopped around subsequently, compared to 8% of those who did very little or no shopping around initially.

4. Vulnerable customers are disproportionately stung

Our analysis shows that customers in vulnerable positions are more likely than the average consumer to stay in their contracts and with their providers. Because vulnerable customers are more likely to be loyal, they are at a greater risk of experiencing the loyalty penalty.

Older broadband users are more likely to stick to the same contract, and therefore experience the loyalty penalty. People aged 65 and over are also more than twice as likely as those under 65 to have been in the same contract for more than 10 years.[24]

Figure 4. Older customers are more likely to stay in their contracts for longer than younger customers



Lower income households are also more likely to experience the loyalty penalty. Households earning less than £7,000 per year are 77% less likely to change contracts in the first 4 years than those on the highest income bracket.[25] Those

[24] 22% of those aged 65 or over say they have been in the same contract for more than 10 years, compared with only 8% of those aged 18 - 64 years old.
[25] Those on the highest income bracket are defined as households earning more than £83,000 per year.

earning between £7,001 and £21,000 are almost 3 times as likely as those earning more than £55,000 to be in their contracts for 10 years or more.[26]

Households earning less than £7,000 per year are **more than twice as likely** to be in their contract for more than **10 years** than those earning more than £83,000

For some vulnerable customers, it can be difficult to expect them to spend lots of time comparing different deals before and after entering a contract and to regularly switch to the most competitive one. For example, those aged 65 and over are nearly twice as likely to have done no shopping around whatsoever before entering their contracts compared with adults under 65.[27] 78% of customers who are at least 65 years old have also done very little or no shopping around since then.

Anita, 65, was informed by her provider that her broadband contract was up, but that she could renew it at a cost of £40 per month. Anita's daughter then recommended another provider who could offer the same service for £19 per month. Anita informed her provider of this. Her provider then offered her the same contract for £22 per month.

Older customers are also less aware that they could avoid the loyalty penalty by renewing or changing their contract. 80% of those aged over 65 say they have never been informed by their provider that they could be saving money by switching to a cheaper deal, compared to 73% younger customers.

People who have experienced or currently have mental health problems are also at a greater risk of experiencing the loyalty penalty. Consumers with experience of mental health problems are 32% more likely than others to think that finding a good deal in markets for essential services is not straightforward. Among our clients, those with mental health problems are twice as likely as our average client to come to us for help on how to find a good deal in phones, TV, broadband and other markets.

[26] 14% of those earning between £7,001 and £21,000 said they have been in the contract for 10 years or more, compared to 5% of those earning more than £55,000.
[27] 25% of those aged 65 or over have done no shopping around before entering their contracts compared with 13% of those aged 18-64 years old.

Recommendations

Across a range of essential markets, including energy, insurance and telecoms, customers are being penalised for their loyalty. After the initial contract period, often providers of these services shift their customers onto uncompetitive tariffs, taking advantage of the fact that loyal customers are unlikely to shop around.

This should be of concern to policymakers. The loyalty penalty suggests that competitive pressures do not apply to large sections of essential markets. But suitable responses will vary, according to specific features of the market and the level of detriment. So while the introduction of a price cap for vulnerable customers in the energy market is important given the size and history of the detriment, different responses may prove more effective in other markets.

In the broadband market, there are number of opportunities to redress the balance and improve outcomes for consumers:

Price comparison websites should include price information beyond the minimum contract period. 60% said they used a price comparison tool to shop around before entering a contract. Given that broadband customers surveyed said they had been with their provider for 4 years on average, price comparison websites should make it easier for people to understand the likely costs of the contract over its lifetime. The Competition and Markets Authority should consider this as part of their market study into digital comparison tools.

The ASA should examine whether broadband providers are displaying pricing clearly on websites and through advertising, including the costs once the minimum contract period has ended. It is currently far too difficult for customers to understand that their broadband contract includes a loyalty penalty. Providers often do not make this sufficiently clear on their websites or in their advertising. Building on the ASA’s success banning misleading broadband adverts which obscured the cost of line rental, the ASA should look again at this market. The ASA should require providers to clearly state the price of broadband after the minimum contract period alongside the initial tariff. As part of this, the ASA could also consider price comparison websites that fall within its remit.

Ofcom should monitor the development of the loyalty penalty and take further action if detriment continues. Encouraging people to switch is only a partial solution to the loyalty penalty, as many consumers stay in their contracts for long periods and pay a steep price for doing so. If providers continue to charge significantly higher prices to loyal customers than to newer customers, Ofcom should conduct further analysis of consumer detriment and take action in the market. Three potential interventions include:

- The requirement for providers to use timely, smart alerts (such as text messages)[28] to inform customers that they are nearing the end of their minimum contract period and that their tariff is about to rise
- Build an understanding and definition of vulnerable customers, including older and lower income groups
- Further thinking into whether additional protections, including price regulations, are necessary to protect vulnerable customers who do not switch to better tariffs after their initial period expires. Ofcom's proposal to cut at least £5 per month off the bills of BT landline-only customers is a welcome intervention for a vulnerable group of customers. Ofcom should remain vigilant to other such pockets of detriment.

[28] Our previous research has showed that this type of disclosure can go a long way in addressing consumer detriment.

Appendix

Methodology

We looked at the cheapest basic broadband contracts offered by providers online. The minimum periods for these contract were 12 months for BT and Sky, 18 months for EE and 24 months for Talk Talk. The prices used in this report are correct as of 10th March 2017.

Providers also offer better speed contracts at higher prices or bundle contracts, but these were not taken into account in this analysis.

We compared the price paid by customers during the initial contract period to the tariff they get automatically switched to once the period has ended. This is different to tariffs offered for renewal of the same contract. We looked at the standard tariff the contract gets automatically rolled on to after the initial contract period if the customer does not renew, upgrade, cancel or switch.

While broadband customers often incur additional costs when switching to a different provider, this is less often the case when they move to a different contract with their existing provider. Moreover, set up costs are part of an additional service customers pay when switching. We have therefore not included them in our analysis.

All providers except Virgin Media had more expensive out-of-contract tariffs for their cheapest basic broadband contracts. However, Virgin Media's cheapest broadband and phone bundle is cheaper than their basic broadband contract, at £32 per month. After a year, the tariff increases by 24% to £40 per month. Virgin Media also has a cheaper broadband, phone and TV bundle for £29 per month, rising to £45 per month after one year. This is a 55% increase and a loyalty penalty of £16. 4 out of the 5 largest providers include a penalty in bundled TV and broadband contracts.

We also looked at how the price of broadband after the initial period is advertised on providers' websites. We looked at the webpage where the out-of-contract price is displayed, the number of times a customer has to click the page to get there from the page where the initial price is first advertised, and the different fonts in which the two prices are advertised. Virgin Media does not include an automatic out-of-contract tariff rise for its 12 month, basic broadband contract. However, this is only communicated to customers if they use the live chat to speak to a Virgin Media adviser or once they reach the confirmation page.

Our analysis was supplemented with a survey run by Populus in January 2017. Populus ran an online survey of 3196 consumers in the energy, telecoms and financial services market. Data were weighted to be representative of the UK population. We also recorded data about the respondent's gender, age, household income, level of education, mental health, region, tenure and ethnic group.

Data table: Full breakdown of charges for cheapest basic broadband contracts

This table compares the initial monthly price of a fixed contract and subsequent monthly price of the 5 largest suppliers' cheapest basic broadband deals as advertised on their website on 10 March 2017. The contract length for the cheapest deal varies across suppliers.

Provider & cheapest basic broadband deal	Monthly tariff during fixed contract period	Monthly tariff after fixed contract period	% increase	Monthly difference	The annual loyalty penalty[29]	The loyalty penalty over 4 years
BT 12 month	£24.49[30]	£40.99	67%	£16.50	£198.00	£594
Virgin Media 12 month	£32.25	£32.25	0%	£0.00	£0.00	£0.00
Talk Talk 24 month	£20.00	£25.50	28%	£5.50	£66.00	£132
Sky 12 month	£18.99	£28.99	53%	£10.00	£120.00	£360
EE 18 month	£21.00	£28.50	36%	£7.50	£90.00	£225

[29] Yearly difference between initial fixed contract period and after fixed contract period
[30] This is a time limited offer.

We help people find a way forward

Citizens Advice provides free, confidential and independent advice to help people overcome their problems.

We advocate for our clients and consumers on the issues that matter to them.

We value diversity, champion equality and challenge discrimination.

We're here for everyone.

citizensadvice.org.uk

Published April 2017

Citizens Advice is an operating name of The National Association of Citizens Advice Bureaux.

Registered charity number 279057.