Excessive prices for disengaged consumers

A super-complaint to the Competition and Markets Authority

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Introduction

Deep, structural price discrimination against disengaged and loyal consumers has been a persistent feature of essential markets for many years. After careful consideration, we have reached the view that the scale of this problem justifies a super-complaint, the first time we have taken such action in seven years.

In support of that complaint, this document sets out Citizens Advice's evidence regarding the failure of competition to make markets work for loyal and unengaged consumers in essential markets. We propose that the CMA in its response should commit to initiating a market study to identify remedies and recommendations that put an end to this practice.

The penalty paid by loyal consumers has been well-established in the energy market. Years of investigation by Ofgem, the CMA and Government have led to a range of new protections for consumers - first capping the cost of prepayment meters,[1] then capping the bills of vulnerable customers[2] and - ultimately - capping the cost of energy for all customers on default tariffs in the market, expected to save consumers £75 a year on average.[3]

But excessive prices for disengaged consumers can be just as high - if not more so - in other essential markets like mortgages and mobile. Often this isn't an increase of just a few percentage points: a home insurance customer, for example, who has been with the same firm for 5 years can pay 70% more than a new customer.[4]

Competition in these markets is often working well for the active, new consumer. The margins companies can earn on these consumers is often low or non-existent, since the best introductory deals track underlying costs closely. But this is only sustained by charging loyal customers unjustifiably high prices.

Across five markets critical to people's lives, we estimate that loyal consumers are overcharged almost £900 a year. This is, in effect, a systematic scam: nobody would **choose** to pay such higher prices - companies charge these prices **solely** in the hope that people won't notice. The scale of this rip-off is vast - billions of pounds, typically taken from vulnerable consumers, undermining people's faith in markets.

None of these markets are *'free'* in a traditional sense and one should expect competition to operate somewhat differently as a result. Some, like broadband and mobile, are built atop a natural monopoly, where competition has only been enabled by

[1] Ofgem, Safeguard tariff (or 'price cap'), April 2017.
[2] Ofgem, Vulnerable customer safeguard tariff, February 2018.
[3] Ofgem, Ofgem proposes price cap to give 11 million customers a fairer deal for their energy, September 2018.
[4] Financial Conduct Authority, Price discrimination and cross-subsidy in financial services, September 2016.

careful market design (the privatisation of BT and the introduction of retail competition in the case of broadband; spectrum auction and regulation in the case of mobile). And all are tightly regulated, in virtue of how essential they are to consumers and the often catastrophic consequences, to consumers and the economy alike, if these markets fail (particularly in financial services).

Many have elements of price regulation already. And all have consumer inertia 'baked in' through long-lasting, automatically renewing contracts that allow price increases at the end of a contract. This inertia - people's tendency to stick with a previous decision - is one of the strongest forces in consumer behaviour. The way choices are designed - in this case, making the status quo contract renewal with a higher price - has a significant impact on behaviour, even if the economic incentives for switching providers are clear. This ability to exploit this behaviour is the principal reason why the loyalty penalty is so widespread and persistent.

Previous attempts to fix the loyalty penalty often ignored this fact, thinking that simply getting companies to inform consumers about switching would be sufficient to get people to focus on their economic incentives. Early attempts failed to have any effect as a result. However, as regulators increasingly focused on identifying how best to overcome behavioural inertia and empirically test interventions, they have steadily improved. A recent test of collective switching in the energy market has appeared particularly promising.

While growing in value, there will always be a limit to the number of people reached by these interventions; even as testing and design has improved, a large number of consumers have remained disengaged. There is still room for regulators to learn from each other about what works best: the difference between the worst and best approaches across sectors is significant. But most interventions have led to a top-end of 5-10% increases in switching. This has led to real benefits for some consumers, but a sizeable problem remains; past efforts have still not been proportionate to its size.

We hope technological innovation may help even more consumers engage in markets. As switching services and architecture improve, and as companies develop products that make better use of consumers' data, so should the number of consumers able to engage, as switching costs go down and the benefits of engagement go up. We are ourselves trialling new tools to combine the technologies of our partners with the unparalleled community-based reach of Citizens Advice. But the success of these tools should not be relied on by policymakers, and the default assumption should be that - without careful planning - technology will benefit those already engaged more than vulnerable people, potentially widening the gap in outcomes.[5]

We therefore conclude that only reforms to how these markets are designed and the rules firms have to follow will lead to systematic improvements for the remaining loyal consumers. There have been welcome signs that regulators are considering bolder

[5] For example, a PwC study estimated that the digitally excluded lost £4.5bn in savings each year: PwC, Champion for Digital Inclusion: The Economic Case for Digital Inclusion, October 2009.

intervention in this regard (such as a potential Basic Savings Rate for cash ISAs). What has been lacking is a proper cross-sectoral approach: something only the CMA is in a position to do.

The existence of these problems and the limited effects of past interventions are not findings that we expect the CMA to find controversial; the loyalty penalty's prevalence among low income and vulnerable consumers is similarly widely accepted and evidenced by regulators, Government and consumer bodies. It is how to fix this that we now look to the CMA to help resolve.

What the CMA should do

As a consequence of its response to this complaint, the CMA should undertake a thorough, cross-sectoral market study into the penalty paid by loyal and disengaged consumers. While we have identified its existence in five markets, this study should consider the loyalty penalty wherever it occurs and propose recommendations and remedies that can be implemented by itself, sector regulators and the Government.

We expect that these will involve some combination of identifying:

- 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.
- What specific protections for low-income and vulnerable consumers who pay the loyalty penalty are necessary.

In certain markets, we have concrete recommendations regarding solutions. In the mobile market, where the rip-off is most blatant, we think the practice of continuing to charge for the handset after the minimum contract term must come to an end. We therefore welcome Ofcom's consultation on how it can end this practice by introducing fairer default tariffs.[6] In others, there may be ways of strengthening existing proposals - examining whether a relative cap on mortgages might reduce detriment in the mortgage market[7] or the merits of strengthening a Basic Savings Rate by (for example) linking it to the Bank of England rate. However, for all remedies, we think it's right for the CMA to investigate the advantages and disadvantages of these approaches in greater detail.

Significant price differentials for loyal consumers are unfair no matter who they affect - no other markets require this peculiar and difficult kind of engagement from consumers every 1-2 years in order not to get ripped off. But these penalties proportionately hit the poorest and most vulnerable in society's budgets the most.[8] Well designed markets

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[6] Ofcom, Helping consumers to get better deals in communications markets: mobile handsets, September 2018.
[7] Citizens Advice, Improving the Mortgage Market, Citizens Advice formal FCA Mortgage Market Study response, August 2018.
[8] See Chapter 2 for more details.

should serve, not punish, these groups. In devising what remedies are appropriate, and in thinking about making any potential trade-offs in designing these remedies, the interests of these groups should be prioritised.

In assessing whether our complaint is justified, the CMA is responsible for investigating whether consumers' interests are harmed by this problem and setting out what action it proposes to take. In light of the complexity of the issues we are raising, we do not expect it to come to a final view in 90 days, which is why we think a cross-sectoral market study is necessary. As a consequence of this study, the CMA should identify what action it can take and what action other bodies such as the FCA, Ofcom and Government need to take.

The CMA may also have recommendations that require direct Government intervention, through legislation or other means. It may also be necessary for the CMA to identify limits on its current powers or in competition law, which make it harder to solve the loyalty penalty. If so, the CMA should identify these limits for Government to solve.

The remainder of this document

This document sets out our best understanding of the severity of these problems in different markets we have studied: broadband, mobile phones, home insurance, fixed-rate mortgages and savings. As noted above, we do not think this exhausts the markets where we should expect to see a loyalty penalty; it is instead where we have found empirically tractable ways of demonstrating it. Any market where customers are automatically placed on a standard rate upon expiry of an initial deal will be a candidate for this structural market failure.

This complaint is made in accordance with Part 1, Section 11 of the Enterprise Act 2002, in our role as a designated consumer body and in relation to a pricing structure that exists across many markets.

While we have amassed a substantial body of evidence regarding the loyalty penalty in support of this super-complaint, we do not regard our analysis as the final word on the size, scale, distribution and economic impact of the loyalty penalty. Indeed, where others have reached different conclusions regarding its precise shape in particular markets, we have reported this as additional evidence. Rather we regard it as evidence that a substantial, systematic and ongoing problem exists in these markets. We expect that the CMA's investigation will focus on solving these problems.

In our view, this is principally justified for the following reasons:

1) **Consumers' interests are harmed.** In particular, long-standing consumers in essential markets frequently overpay for goods and services. 8 in 10 people are currently charged significantly higher prices for remaining with their existing supplier in one or more essential market. Our best estimate of the cost of loyalty in these markets is £4.1bn per annum. **Section 2** of this document sets out our

evidence on a) why the loyalty penalty occurs and b) the total size of the detriment for loyal consumers.

2) **This penalty is disproportionately paid by vulnerable and low-income consumers.** While the penalty is unjustified in general for these consumers, in certain markets we reference in this complaint, they also make up a disproportionate number of the consumers who pay this penalty. **Section 3** of this document sets out our evidence regarding the impacts on lower income and vulnerable consumers.
3) **Competition is not always working effectively in these markets.** For all disengaged consumers, competition is not leading to tolerable outcomes. In the retail energy market, the CMA found that there were market features (particularly related to disengagement) that led to adverse effects on competition. **Section 3** makes the case that similar dynamics may be present in other markets, making them worthy of investigation.
4) **Past regulatory action has not been proportionate to the scale of the challenge**, apart from in the energy market. **Section 4** sets out an overview of preceding regulatory actions, that have principally tried to encourage switching. The message from these interventions is that, while they have - sometimes, though not always - worked at the margins, they have generally increased switching by only modest amounts. There is little market-wide evidence that any remedies have led to persistently and significantly higher levels of switching.

We conclude by offering recommendations on *how* the CMA might go about remedying the situation.

Much of this report is derived from our past research and evidence, particularly our reports on the loyalty penalty in specific markets and our whole-of-market report, 'The cost of loyalty'.[9] All our past reports are included as appendices.

[9] Citizens Advice, The cost of loyalty: exploring how long-standing customers pay more for essential services, February 2018.

Types and sources of evidence

Citizens Advice has gathered data and conducted research into the loyalty penalty since April 2017. We have published 5 research reports on the loyalty penalty in essential service markets, along with a number of press releases and consultation responses:[10]

- Exploring the loyalty penalty in the broadband market[11]
- Exploring the loyalty penalty in the mortgage market[12]
- The insurance loyalty penalty[13]
- The cost of loyalty across 6 essential markets[14]
- Reviewing bundled handsets[15]

These outputs made use of both qualitative and quantitative research techniques, summarised below:[16]

- We conducted 2 nationally representative online surveys in January and June 2017. Populus ran surveys of 3,196 and 3,070 people respectively in the energy, telecoms and financial services markets. Data were weighted to be representative of the GB population. Data about the respondent's gender, age, household income, level of education, mental health, region, housing tenure and ethnic group were also recorded. Populus is a founder member of the British Polling Council and abides by its rules.[17]
- A final nationally representative poll of 3,030 adults in Great Britain was conducted by ComRes for Citizens Advice, 18-25 July 2018. Unless stated otherwise, all quoted polling results are from this latest poll.
- Citizens Advice researchers collected information on tariffs and-out of contract prices via desk research to estimate the size of the loyalty penalty in the broadband and mobile handset markets.
- They also audited advertising behaviour across major providers in each market using desk-based research, including contacting providers by live web-chat and telephone.
- Case studies come from evidence forms completed by local Citizens Advice offices, and data collected by the Citizens Advice consumer service. All reports have been anonymised to maintain confidentiality.

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[10] Citizens Advice, Modernising consumer markets: Citizens Advice formal consultation response, 2018; Citizens Advice, Citizens Advice responds to the FCA's move on the loyalty penalty, 2018; Citizens Advice, Improving the Mortgage Market, July 2017.
[11] Citizens Advice, Exploring the loyalty penalty in the broadband market, April 2017.
[12] Citizens Advice, Exploring the loyalty penalty in the mortgage market, July 2017.
[13] Citizens Advice, The insurance loyalty penalty: unfair pricing in the home insurance market, November 2017.
[14] Citizens Advice, The cost of loyalty: exploring how long-standing customers pay more for essential services, February 2018.
[15] Citizens Advice, Hung up on the Handset. An investigation into sales practices in the mobile phone market, April 2016.
[16] See Appendix A for full details.
[17] The csv files for the three national surveys are an appendix to this complaint.

- Quotations from consumer interviews and open text questions in our national surveys have also been used throughout the report as further qualitative evidence.
- We have analysed data collected by the FCA, Ofcom, Ofgem, Bank of England and the Office of National Statistics. We have also used information published by other external sources. A full list can be found in the technical and data appendices.

Using these sources, we have reached our best estimate of the size, scope and impact of the loyalty penalty. It is not intended as the final word, and different assumptions and methodologies can (and have) led to different results. However, combined with evidence from other consumer bodies and regulators, our findings constitute a strong case for an in-depth investigation of possible solutions to the problem.

1. The loyalty penalty: whole-of-market findings

The loyalty penalty - the difference between what loyal and new consumers pay for the same service - is an accepted feature of many markets. In broadband and home insurance markets, the penalty occurs when customers default onto a more expensive standard tariff once their original contract comes to an end. In savings and mortgages, long-standing customers are moved to poorer value interest rates. In handset inclusive mobile contracts, providers often continue to charge people who don't shop around the same amount even after they have paid off the full cost of the handset.[18]

This section sets out:

- How many people pay a loyalty penalty
- How much those people are likely to pay
- Consumer perceptions and awareness of the loyalty penalty

While this section provides key methodological details underpinning our estimations, Appendix A provides a fuller overview of how we have estimated the loyalty penalty in each market.

How many people pay a loyalty penalty?

This section provides our best estimate of the extent of the loyalty penalty in five essential markets. Our most recent polling finds that 8 in 10 people responsible for household bills are paying the loyalty penalty in at least one market.

Table 1: Our polling on percentage of people likely to be paying a loyalty penalty in five markets

Market	Percentage
Mobile (including handset)	34%
Broadband	43%

[18] While SIM-only contracts make up a substantial proportion of the market, contracts including both mobile service and the cost of the handset make up nearly three quarters of the post-pay mobile service market. Ofcom, Pricing trends for communication services in the UK, May 2018.

Home insurance	47%
Fixed-rate mortgage[19]	10%
Savings account	37%
Total paying a loyalty penalty	**80%[20]**

How much is the loyalty penalty?

A customer experiencing the loyalty penalty in all five markets in question will be paying up to £877 more for these services each year. This is equivalent to over 3 months' worth of food for the average household.[21]

Table 3 shows our previous estimates of the loyalty penalty in five different markets, with a summary of the methodological approach used. Appendix A provides a fuller account of these methodologies.

Table 2: The cost of paying the loyalty penalty for one year in five markets; Citizens Advice research

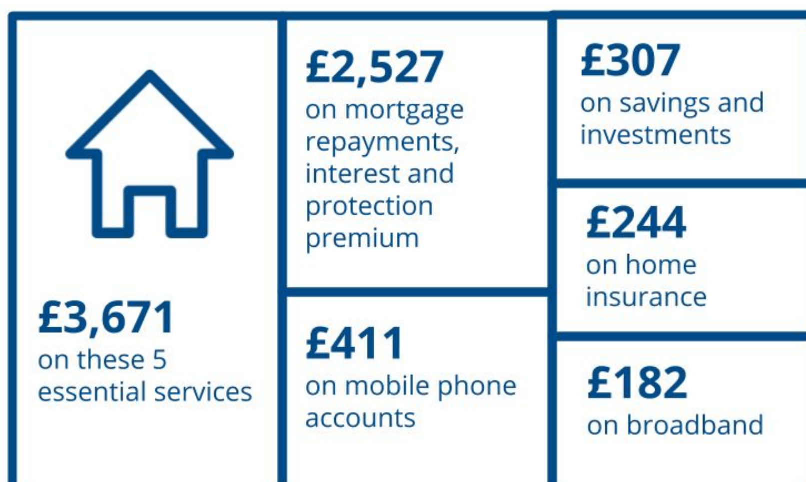
Market	Penalty	Summary of methodological approach
Mobile (including handset)	£264[22]	Amount overpaid when people remain on a contract for a year after they have paid for the handset, if paying the average monthly penalty.
Broadband	£113[23]	Difference between the cheapest basic broadband contract and the price customers pay after the initial contract period ends.
Home insurance	£13[24]	Average difference between the initial price a customer pays, and the price offered on renewal after 1 year, based on the average cheapest combined premium. This penalty increases over time.

[19] This refers to specifically 2, 3 and 5 year fixed-rate mortgages.
[20] Percentages do not sum due to many consumers paying a loyalty penalty in multiple markets.
[21] ONS, Family spending in the UK: financial year ending 2017, January 2018.
[22] Citizens Advice, Mobile phone networks overcharging loyal customers by up to £38 a month, October 2017.
[23] Citizens Advice, Exploring the loyalty penalty in the broadband market, April 2017.
[24] This is the amount overpaid on a combined policy renewed after 1 year. In our nationally representative survey of British households, 57% of respondents had a combined policy. This figure was calculated using data from the FCA and the AA British Insurance Premium Index. Further details in Appendix A and in specific broadband briefing.

Fixed-rate mortgage	£439[25]	Difference between the amount an average customer pays after they are moved from a 2 year fixed-rate mortgage to a Standard Variable Rate (SVR), and the amount they would pay as a new customer with a fixed rate.
Savings account	£48[26]	Difference between interest earned on a 1 year fixed-rate cash ISA taken out in March 2016, and the interest earned when moved to a variable rate in March 2017.
Total penalty	£877	

Figure 1 shows how this compares to the amount that households spend on these five essential services in general (£3,671).

Figure 1: Each year, the average household spends:



Source: Citizens Advice analysis of ONS data.[27]

Table 3 shows the implied revenue covered by the loyalty penalty and the total number of households we believe are spending at least the amount above.

[25] Citizens Advice, Exploring the loyalty penalty in the mortgage market, July 2017.
[26] This refers to the loyalty penalty for cash ISAs. Given the range of different savings accounts available, this focuses on cash ISAs because they are a type of savings account that many people have and about which there is robust data. Calculated by Citizens Advice using average variable and 1 year fixed cash ISA monthly interest rates from March 2017, as published by the Bank of England, and the average balance in ISA accounts as published by HMRC.
[27] ONS, Living Costs and Food Survey, January 2018.

Table 3: Total spent on the loyalty penalty

Market	Number affected	Cost of the penalty
Mobile handset	3,965,000 adults	£473,300,000
Home insurance	12,350,000 households	£708,500,000
Broadband	11,300,000 households	£1,277,000,000
Savings	n/a[28]	£1,136,000,000
Mortgages	1,200,000 households[29]	£526,800,000
Total		£4,122,000,000[30]

Other evidence on the size and scale of the loyalty penalty

In two markets, regulators have subsequently made a different estimation of both size and scale. In the mortgage market, the FCA found that 800,000 would have benefitted from switching, foregoing a potential saving, on average, of £83 every month (£996 if paid for a year).[31] In the broadband market, for dual-play customers, Ofcom has found that the loyalty penalty is somewhat lower (£84).[32]

Evidence on the **number of people** paying the loyalty penalty:

- Ofcom Pricing Trends found that 1.5 million mobile customers whose contract includes a handset are still paying the same price after the end of their minimum contract period.[33]
- Ofcom has also found that, after the initial contract period has ended, broadband prices increase by an average of 20%. The regulator noted that the growing complexity of the market can make shopping around confusing for consumers and can lead them to disengage from the market.
- Analysis by the FCA in 2015 found that home insurance premiums for customers who have stayed with the same firm for five year are on average 70% higher than those for new customers.[34]

[28] FCA data did not enable an accurate estimation of people affected in this market.
[29] Due to calculation method of £437, figures from Exploring the loyalty penalty in the mortgage market used.
[30] Numbers do not add up due to rounding. For the purposes of this report, all figures have been rounded to 4 significant figures.
[31] FCA, Mortgages Market Study: Interim report, May 2018.
[32] Ofcom, Pricing trends for communications services in the UK, May 2018.
[33] Ofcom, Pricing trends for communications services in the UK, May 2018. For an explanation of the discrepancy between our figure and Ofcom's estimate, see Appendix A.
[34] FCA, Occasional Paper No.12, December 2015. Data from three home insurance companies, not market wide.

- The FCA savings market study found that over half of people (58%) had been with their banking provider for ten years or more, with 15% remaining with their provider for five to ten years. Only 4% had been with their main banking provider for less than a year.

Evidence on the **size** of the loyalty penalty:

- The FCA found that, in 2013, approximately £160 billion of easy access savings accounts earned an interest rate equal to or lower than the Bank of England base rate of 0.5%.[35]
- USwitch research found that broadband consumers who are on expired contracts overpay by £105 a year. This research also found that fibre customers miss out on average annual savings of £79.[36]
- Analysis by the Social Market Foundation found it costs on average £92 more if a consumer stays with the same provider at the end of a mobile contract, and £113 more if a consumer stays with their broadband provider after the initial contract has ended.[37]
- Which? found that people who haggle with their insurers and telecoms providers, and who switch energy provider, save up to £725 per year.[38]
- More recently, Which? found that customers with combined home insurance policies owned for longer than a year were paying, on average £75 (38%) more annually than new customers. For contents cover, existing customers paid, on average, 32% more than new policyholders.[39]
- Analysis by Moneyfacts in 2017 found that those approaching the end of a two-year fixed rate mortgage deal faced the highest rate jump in eight years if they chose to revert instead of re-mortgage, at an average cost of £2,000 per year.[40]

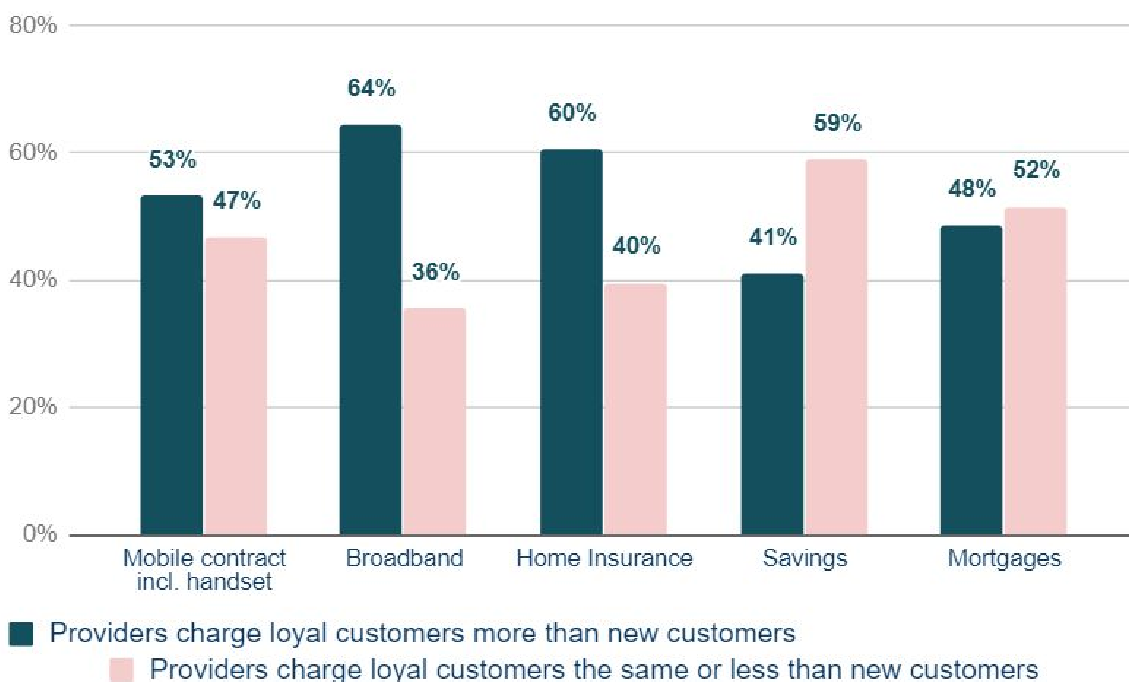
Consumer perceptions and awareness of the loyalty penalty

Our polling shows that awareness of the loyalty penalty varies by market, but that a minimum of 41% of consumers in each market are aware. Public awareness of the

[35] FCA, Cash savings market study report, January 2015.
[36] USwitch, Press release: UK broadband users fork out £1.5 billion a year for inflated out-of-contract charges as prices rise 38% in just five years, February 2017.
[37] Social Market Foundation, Stick or Switch? Making markets fairer and more competitive, October 2017.
[38] Which?, Which? research reveals that loyal customers are being ripped off, December 2017.
[39] Which?, Loyal home insurance customers exploited with excessive premiums, August 2018.
[40] Moneyfacts, Motivation to remortgage hits 8 year high, March 2017.

loyalty penalty varies between markets, with people being up to 23% less likely to expect it in financial services, like savings accounts, than in markets like broadband.[41]

Figure 2: Awareness of the loyalty penalty across the five markets



Source: Citizens Advice analysis of ComRes survey data, 2018.

Some groups are less likely to spot the loyalty penalty than others. Our most recent research finds that those in social grade DE are significantly more likely to say they 'don't know' whether long-standing customers pay more or less than newer customers.[42] Older people are significantly more likely to think that long-standing customers pay the same price as newer customers for their savings account (34% of those aged 65+ compared to 25% of those aged 18-24). This trend can be observed across other markets in a less pronounced fashion.

Spotting the loyalty penalty often requires a good understanding of the market. But in many cases, people do not have this. The FCA's Cash Savings Market Study, for example, found that consumers demonstrate 'widespread misunderstanding and unrealistic expectations about how much variable rates could change'.[43] In the home insurance market, it is difficult to find any price information without searching for a specific quote. It is also difficult to understand what is driving future price changes. And Ofcom found

[41] Citizens Advice analysis of ComRes data on whether British adults thought long-standing customers are likely to pay more or less than newer customers. Bases vary by market and exclude those who answered 'Don't know'.
[42] 33% of those in the DE socio-economic grade category reported they didn't know whether long-standing customers paid more or less than new customers, in comparison to only 20% of those in the AB grade.
[43] FCA, Cash savings market study report, January 2015.

that more than half of consumers (57%) who were outside their minimum contractual period, or were unsure of their contract status, did not realise that potential savings could be made by switching providers or signing up to a new contract with their existing provider.[44]

Consumers' trust in existing providers

The CMA has found that people tend to trust their own banks and energy suppliers more than they trust others, and this may be a barrier to switching.[45]

Our 'The cost of loyalty' report found that trust is a barrier to leaving contracts across essential services. This is echoed in our recent research, with the most popular reason respondents chose for remaining on their current contract was 'I trust my provider', followed by 'I think I'm on the best deal available'.[46] Since more than 4 in 10 people aren't aware of the loyalty penalty, this is perhaps unsurprising.[47]

However, in many cases, such perceptions may be misplaced. While 1 in 3 mobile handset customers stayed because they think they have the best deal available, 59% of these people have been on their contract for longer than 2 years, and are therefore likely to be paying a loyalty penalty.[48] In fact, 1 in 3 people who are likely to face the loyalty penalty in the mobile handset, broadband, mortgage or home insurance markets, believe they are on the best deal available.[49] This suggests people don't have good reason to trust their supplier. And of the 34% of people who have remained on their current broadband contract because they trust their provider, 3 in 4 are likely to be paying a loyalty penalty.

Case study:

Wilson is retired and came to Citizens Advice when he received an unexpectedly high bill. He has been with his mobile provider for many years and contacted them to find out if he could get a loyalty discount. He was told that he could switch onto a cheaper plan as he never exceeded 500 minutes in calls per month. His plan would go down from £11 per month to £7.90. The adviser didn't tell him what charges he'd incur if he exceeded 500 minutes per month, and he received nothing in writing to confirm his

[44] Ofcom, Pricing trends for communications services in the UK, May 2018.
[45] GFK for the CMA, Personal Current Account Investigation and Energy Market Investigation, 2015.
[46] Analysis of ComRes data on the question: 'You said you have been in your contract for a year or more. Why have you stayed with each of the following essential service contracts?' Respondents could select more than one option. Base sizes vary by market.
[47] Citizens Advice analysis of a 3,030 participant-weighted sample of British adults answering whether long-standing customers pay more or less than new customers across energy, mobile (contracts including handsets), broadband, home insurance, savings and mortgage markets.
[48] We have used 2 years as the timescale here because the longest handset contract found in our desk research in this market was a 24 month contract. It is therefore likely that anyone who has had a mobile handset contract for longer than this is being overcharged.
[49] In the savings market, 20% of those likely to be paying the loyalty penalty think they are on the best deal available.

new plan. His first bill was for £66.56 as he exceeded 500 minutes. Wilson would not have thought to change his plan if his provider hadn't suggested it, but assumed they'd have his best interests in mind as a loyal customer. He may have been better off changing provider entirely instead of being loyal.

The unfairness of the loyalty penalty

The vast majority of people think that the loyalty penalty is unfair. In our polling, 89% of respondents think providers of essential services should charge loyal customers the same or less than new customers. This held true across each market tested in our polling, though variations exist.

> "Service providers should recognise their customers' loyalty by charging long-standing ones less than they charge newer customers. Some service providers (not those that are monopolies!) have only continued to exist because of the loyalty of their [long-standing customers]"
> *Karen, 60.*[50]

9 in 10 (90%) respondents to the research agree that essential service providers should inform their existing customers when they are eligible for a better deal than the one they currently have, with 67% strongly agreeing (as we note below, this is rarely sufficient for achieving a well-functioning market).

[50] Response to our 2018 survey question 'Please provide any thoughts you have in the box below on whether it is fair for providers of services such as energy, banking, phone and broadband to charge long-standing customers more than, less than, or the same amount as newer customers.'

2. Impact of the loyalty penalty on vulnerable and low income consumers

This section sets out the impact of the loyalty penalty on different demographic groups:

- Older people
- People with mental health problems
- People on low incomes
- By level of education

Previous Citizens Advice research has shown that those in vulnerable states find it particularly difficult to engage with essential service markets.[51] We are not alone in this finding:

- Research by the FCA and the National Audit Office (NAO) has found that engagement in essential markets is particularly difficult for those in a vulnerable or insecure state due to the complexity of tariffs and information.[52]
- The Competition and Markets Authority (CMA) investigation into the energy market found low income households were less likely to have switched energy supplier between 2011 and 2014.[53]
- Studies by Bristol University and the Social Market Foundation find that lower levels of switching are the biggest determinant of the poverty premium - the additional amount that poorer people pay for the same goods and services.[54] [55]
- Evidence from a 2009 PwC report demonstrates that significant savings are lost by digitally excluded households unable to use digital comparison tools and online transactions.[56]

As a result, particular vulnerable groups, such as those on low incomes, older people, people with health problems and those with lower levels of formal education, are particularly likely to struggle with shopping around and switching, and are therefore less likely to drive competition. Because they are more likely to be digitally excluded or have lower levels of digital skills, vulnerable consumers are less likely to benefit from new

[51] Citizens Advice, Joining the Dots: integrating practical support in mental health settings in England, October 2017.
[52] NAO, Vulnerable consumers in regulated industries, March 2017; FCA, Consumer Vulnerability, February 2015.
[53] 35% of those whose household incomes were above £36,000 had switched supplier in the last three years, compared with 20% of those with household incomes were below £18,000. CMA, Energy market investigation: Final report, June 2016.
[54] Davies, Finney and Hartfree, University of Bristol, Paying to be Poor, November 2016.
[55] Social Market Foundation, Measuring the Poverty Premium, March 2018.
[56] PwC, Champion for Digital Inclusion The Economic Case for Digital Inclusion, October 2009.

digital tools. These people are likely to experience the financial impact of the loyalty penalty disproportionately, suggesting that greater protections are likely necessary for some of these groups.

Older people and the loyalty penalty

Compared to 18-64 year olds, people who are 65 and over are more likely to pay a higher price for the same service in nearly all of the markets focused on in our report.[57]

People aged 65 or over are also more likely to have done no shopping around before entering into a contract than those aged 18-64, across broadband, mortgages, mobile contracts, home insurance and savings accounts.[58] Over 8 in 10 (87%) of over 65s pay the loyalty penalty in at least one market in comparison to 72% of those aged 18-34.[59]

Case study:

Nour, 72, came to Citizens Advice after struggling to use online comparison sites without an email address. Our adviser was able to contact providers using the telephone, but those with the greatest savings refused to go any further unless the client had an email address. The provider they ultimately chose was linked to their current provider, and therefore already had their account details. They were also willing to deal with a client who didn't use an email or have access to the internet. Our local adviser pointed out to the other companies that they are discriminating against people, often older adults, who don't have an email account, and preventing them from accessing better deals.

It may be that those aged 65 and over are more likely to face the loyalty penalty because they are less able to choose the best deal and more likely to stick with the status quo in complex essential service markets. Evidence shows that older people are less likely to make optimal decisions when faced with many options,[60] and are more likely to defer choices when faced with complexity.[61]

Additionally, Age UK has demonstrated that older adults often have a reduced digital capability compared with younger people, with two-thirds of people aged 75 and over, and 3 in 10 aged 65 to 74 not using the internet.[62] Doteveryone research also echoes

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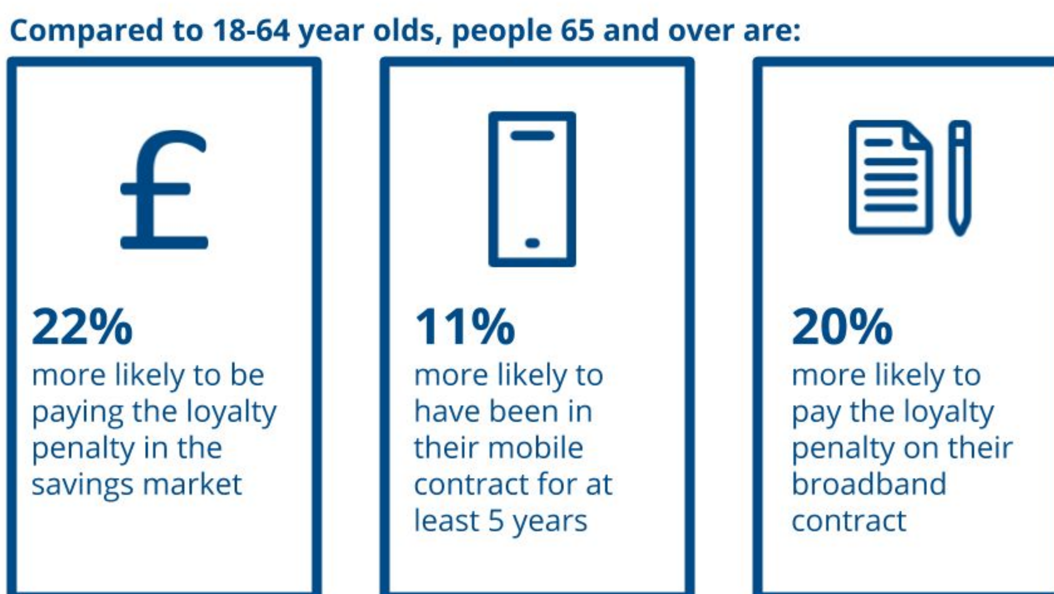
[57] Older people are more likely to pay the loyalty penalty across broadband, home insurance and savings, but are less likely to pay the penalty in mobile and mortgage markets, due to the nature of those markets.
[58] Citizens Advice, The cost of loyalty, February 2018.
[59] 87% of people over 65 from our 3,030 weighted national survey were paying the loyalty penalty in at least one of five markets (mobile, broadband, home insurance, savings and energy). Mortgages have not been included due to skewing effects.
[60] Besedes, T. et al., 'Age Effects and Heuristics in Decision Making', Review of Economics and Statistics, 2012.
[61] Chen, Y. et al., 'Age Differences in Trade-off Decisions: older adults prefer choice deferral', Psychology and Ageing, 2011.
[62] Age UK, Later life in a digital world, 2015.

this, showing that less than half of those over 65 have basic digital skills,[63] which may prevent older people from using price comparison tools - the most common way of shopping around.[64]

These findings are also reflected in a 2017 CMA report, expanding on the ways in which digital comparison tools, such as price comparison websites, can lower costs for consumers and increase supplier competition.[65] This report goes on to explain that service providers can choose to offer better deals to digitally savvy consumers than to those who are less digitally savvy, and vulnerable consumers, particularly older people and those on lower incomes, are less likely to have access to the internet. Therefore, those without access to, or those with less understanding of digital technologies may not be able to make full use of the benefits of such methods of shopping around. The repercussions of this digital exclusion are explained in a Government Digital Service (GDS) report, with those who are offline paying over £500 a year more for services and goods, on top of the social knock-on effects of reduced ability to keep in touch with family members and friends.[66] The GDS report also emphasises that, because of this, beyond financial implications, being online makes people feel part of modern society and helps to tackle social isolation.

Figure 3: Older people are more likely to pay the loyalty penalty



Previous research by Citizens Advice found that those over 65 are disproportionately likely to ask Citizens Advice for help with home or vehicle insurance issues (21% vs 14% overall).[67] Over half of those aged 65 and over are paying the loyalty penalty on their

[63] Doteveryone, Basic Digital Skills, UK report, 2015.
[64] Citizens Advice, Exploring the loyalty penalty in the broadband market, April 2017.
[65] Competitive Markets Authority, Digital comparison tools market study, September 2017.
[66] Government Digital Service, Government Digital Inclusion Strategy, December 2014.
[67] Citizens Advice, The insurance loyalty penalty, November 2017.

home insurance, while 45% of those under 65 are likely to pay the penalty in this market.[68] Additionally, those over 65 are also more likely to have had their policy for a long time, with 26% of over 65s having had their current policy for over 5 years in comparison to only 16% of 18-64 year olds.[69]

Older broadband users are more likely to stick with the same broadband contract, and therefore experience the loyalty penalty. Almost 6 in 10 customers aged 65 and over are paying the broadband loyalty penalty, having been in their contract longer than the minimum period, compared to just over a third of those under 65.[70]

Mental health and the loyalty penalty

Citizens Advice research finds that shopping around and switching may prove more difficult for those with mental health problems. In our survey, 15% of those who have experienced a mental health problem in the last 12 months think it's too difficult to switch contracts in essential service markets, compared to just 5% of those who have not. And while nearly 1 in 10 (8%) of those who haven't recently experienced mental health problems think it's difficult to switch mortgage contract, this rises to 28% among those who are experiencing mental health problems with a severe impact.[71]

> "This was before I wasn't well, so I would've been able to look properly on the internet and to see what's best for us...I don't think I could [now]. I mean I can go on the laptop sometimes, but I just get a bit confused. Like I forget what I'm doing...I get a bit lost. I'll be doing something and then my thoughts trail off and I can't remember what I was doing in the first place and I can't figure out like, you know, why is it this much, why is it that much."[72]

There is also a cyclical link between financial difficulty and mental health, with 72% of people experiencing mental health problems stating that their poor mental health had made their financial situation worse, and 86% reporting that their financial situation had made their mental health problems worse.[73] Our data shows that those on low incomes

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[68] 54% of those we surveyed aged 65 and over are likely to be paying the loyalty penalty, in contracts to 45% of under 65 year olds. Citizens Advice analysis of ComRes data.
[69] Citizens Advice analysis of a ComRes survey of 3,030 British adults, weighted nationally.
[70] 59% of those aged 65 and over have been in their broadband contract longer than 2 years, compared to 38% of under 65 year olds, as analysed from a nationally weighted ComRes survey of 3,030 British adults.
[71] 28% of those who responded "I experienced mental health problems that reduced my ability to carry out activities by a lot" (in the last 12 months), also reported that they thought switching mortgage contracts was too difficult. For evidence showing the negative impact poor mental health has on financial capability, see The Money and Mental Health Policy Institute, 'Seeing through the fog': How mental health problems affect financial capability, 2017.
[72] Extract from Citizens Advice interview transcript.
[73] Analysis of a Money and Mental Health survey of nearly 5,500 people with experience of mental health problems forming a self-selecting sample. Money and Mental Health Policy Institute, 'Money on your mind', June 2016.

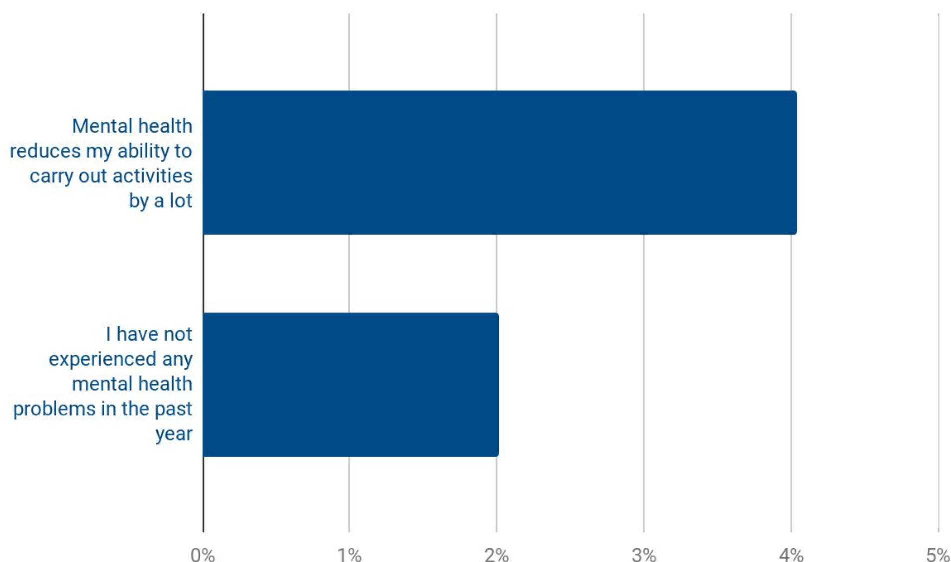
are 20% more likely to have experienced a mental health problem,[74] and more than 4 in 10 of those who report their mental health significantly impacts their day-to-day life are on low incomes (earning under £21,000). Research by Mind reflects this, showing that nearly half (45%) of respondents to a survey of people with mental health problems in England and Wales live on less than £200 a week, and three-fifths of respondents reported feeling confused about their finances.[75]

The most commonly reported mental health problems, according to Mind, are depression and anxiety, which were reported by 61% and 45% of those in our survey who had experienced mental health problems in the last 12 months respectively. Often depression can cause a lack of motivation, which makes financial management difficult, and people with depression exhibit moderate planning deficits, which may not resolve even if symptoms reduce.[76] Poor planning and decision-making can be particularly problematic when making decisions about long-term financial products such as mortgages, or certain types of insurance.[77] Similarly, those suffering from anxiety are likely to struggle with complex financial tasks, such as comparing different essential service tariffs or discussing contract details over the phone. It is clear that for those with mental health problems, managing their finances and service contracts will prove much more challenging than for those without mental health problems, and this challenge can prove a particularly costly one.

People who have experienced mental health problems that impacted their daily life are less likely to have a home insurance policy than those who reported their mental health problem had no impact (18% compared to 11%). Additionally, as seen in Figure 4, those with mental health problems that have a severe impact are twice as likely not to remember when they renewed their policy compared with those who have not experienced a mental health problem in the last year. This illustrates the complications with managing finances and consumer decisions for those with mental health problems.

[74] 59% of those earning less than £7,000 reporting having a mental health condition in our nationally weighted survey of 3,030 British adults, in comparison to only 39% of those earning more than £55,000.
[75] Non-random sample of people with mental health problems in England and Wales. Mind, Still in the red, 2011.
[76] Money and Mental Health Policy Institute, Mental Health Problems And Financial Capability, January 2017.
[77] The Money and Mental Health Policy Institute, 'Seeing through the fog'; How mental health problems affect financial capability, 2017.

Figure 4: Proportion of people who don't remember when their home insurance policy started



Source: Survey conducted by ComRes for Citizens Advice. Base: 3,030

Telecoms can be a particularly difficult market to navigate for consumers with mental health problems.[78] Among our Citizens Advice 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.[79]

Within the broadband market, consumers with mental health problems were more than twice as likely to say their main reason for staying in their contract was because switching was too difficult compared to those without mental health issues (17% and 7%). Additionally, nearly 1 in 5 (17%) of those with mental health problems that impacted their daily life said that they found the process of switching broadband contracts time consuming, compared to just 9% of those who had not experienced mental health problems. This is further evidence that consumer markets are much harder to navigate and engage with for people who experience mental health problems, in comparison to those who have not.

Additionally, for those with disabilities and long-term health conditions, life is already more expensive in a multitude of ways. For example, research by Scope has found that disabled people, on average, face extra costs of £570 a month related to their impairment or condition.[80] Similar to mental health issues, nearly a third of those who reported having a disability said they renewed their most recent policy without looking for better deals elsewhere, compared to 1 in 5 of those who did not report a disability.[81]

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[78] Citizens Advice, Essential service markets and people with mental health problems, May 2018.
[79] Citizens Advice, Exploring the loyalty penalty in the broadband market, April 2017.
[80] Scope, The disability price tag, 2018.
[81] Citizens Advice, The insurance loyalty penalty, November 2017.

Case study

Alex, 43, has tetraplegia and insured his car with a company that specialises in insurance for disabled people. A premium of over £800 per year seemed steep but he assumed that, as he required cover for being over 25, this was reasonable. When renewing his policy, the company stated the annual cost would rise 23% to over £1,000. After searching online, Alex found an identical policy for £268 per year. Despite contacting the company 3 times he received no response. It was only when he informed the Citizens Advice consumer service of his issue that the insurance company responded, and offered to price match the nearly £800 cheaper deal.

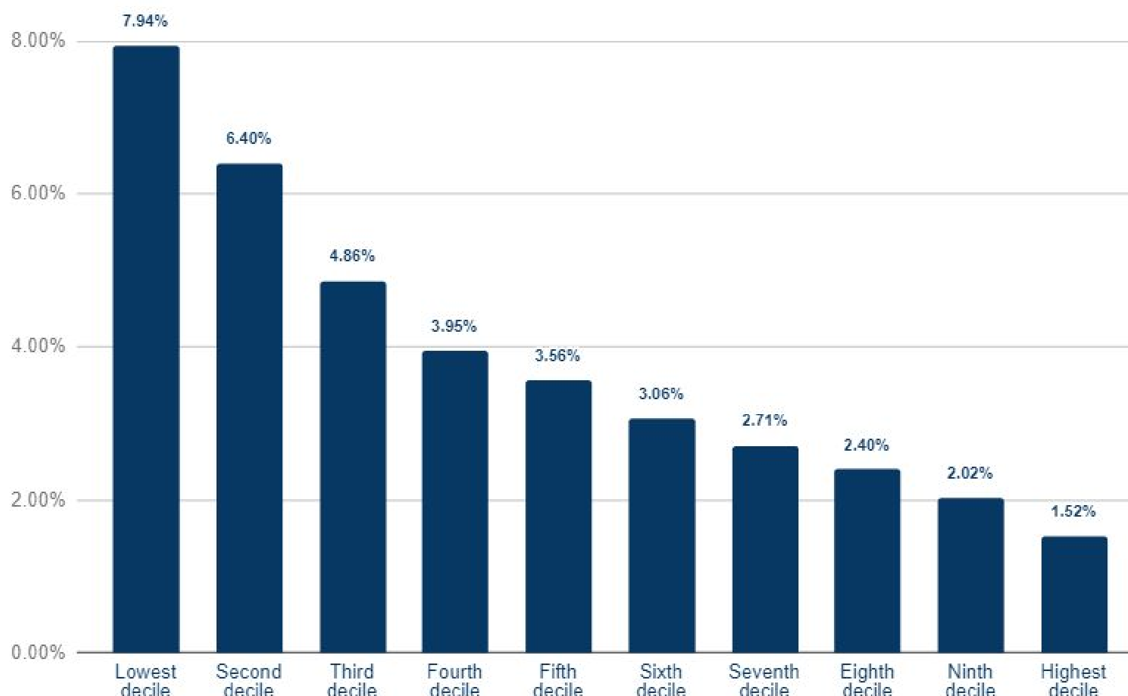
Alex said that he struggles to actively shop around for competitive quotations due to his condition. He believes many other disabled people are in the same situation, and says that this is unfair and unethical treatment of people with disabilities.

Low income and the loyalty penalty

Our most recent polling indicated that similar proportions of low, medium and high income earners pay the loyalty penalty in at least one market.[82] However, those from low income households lose a greater proportion of their household expenditure to the loyalty penalty in comparison to higher earners. For those in the lowest income decile, paying the loyalty penalty across all five markets mentioned above would cost them almost 8% of their household expenditure annually, in comparison to less than 2% for those in the highest 10%, as seen in Figure 5. Davies, Finney and Hartfree (2016) echo that additional costs for the same service may be experienced across the income spectrum, but they place a disproportionately high strain on low income households' resources.[83]

[82] Cross-sector analysis using a weighted sample of 3,030 British adults showed that 78% of households earning under £21,000, 82% of those earning £21,000-£41,000, and 81% of households earning over £41,000 pay the loyalty penalty in at least one of the five markets (mobile, broadband, home insurance, savings, and energy).
[83] Davies, Finney and Hartfree, University of Bristol, Paying to be Poor, November 2016.

Figure 5: Loyalty penalty accounts for higher proportions of low income households' expenditure (by decile group)



Source: Office for National Statistics, January 2018 [84]

Evidence from our survey suggests people on lower incomes are more likely to struggle with shopping around and switching. In addition, previous research has shown that there are cognitive and behavioural biases associated with living on a low income that make it more difficult to actively engage in consumer markets. For example, those on low incomes may not be switching due to the effects of the 'scarcity mindset', which refers to the tendency of those who are worried about their financial situation to have less cognitive capacity to devote to other areas of their life such as managing services.[85] This may create a barrier for low income households being engaged consumers, with 42% of those earning under £21,000 reporting they don't have the time to shop around for good deals in these services.[86] The scarcity mindset may also explain why social renters are nearly 10% more likely to pay the loyalty penalty in at least one market compared to private renters, and more than 20% more likely to pay it than those who live in a home without paying rent.[87]

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[84] This graph uses ONS data to demonstrate how paying the loyalty penalty in all five markets would map onto the household expenditure of households in each income decile. As there is currently no data on the incidence of the loyalty penalty across income decile groups, and few households pay the penalty across every market, this is purely for illustrative purposes. Office for National Statistics, Family spending in the UK: financial year ending 2017, January 2018.
[85] Sendhil, Mullainathan and Eldar Shafir, *Scarcity: The true cost of not having enough*. 2014.
[86] Citizens Advice analysis of responses to the statement 'I don't have time to shop around' from a ComRes survey of 3,030 British adults. This includes both 'Strongly agree' and 'Slightly Agree'.
[87] Rent free is defined here as those living in a house or flat without paying rent, and is distinct from those who own a home outright without a mortgage. Citizens Advice analysis of 2018 ComRes nationally weighted survey data (base: 3,030).

These extra costs incurred as a result of both behavioural and circumstantial factors can be explained as part of the 'poverty premium', which Davies, Finney and Hartfree (2016) describe as the extra costs poor people end up paying for the same essential goods and services compared to those not in poverty.[88] They identified six higher cost areas as forming the poverty premium, which included insurance and telecommunications, in addition to fuel costs and other expenses. The loyalty penalty sits across both demand and supply-side factors identified within the poverty premium, reflecting facets such as risk aversion surrounding switching supplier, and general market failures and competitive practices. The University of Bristol report also outlines compounding factors such as financial capability and digital exclusion, the former of which has been touched on above in regards to the scarcity mindset. These factors should be taken into consideration when decision-makers consider consumer policies affecting low income households.

A report by the Social Market Foundation emphasises that vulnerable people, such as low income households, are particularly susceptible to bad deals in consumer markets.[89] Greater proportions of household expenditure lost to the loyalty penalty penalises low income families and may cause them to face higher-than-average rates of inflation during periods when the cost of essentials such as utilities are rising at a faster rate than headline inflation. This results in a disproportionate impact on and harm to those with lower incomes.

In regards to market specific findings, those on low incomes are less likely to actively engage in the market when their home insurance policy renews, possibly due to reduced cognitive capacity or expectation of claims being rejected.[90] People with an annual income of £7,000 or less who had some form of home insurance were nearly 4 times more likely to say they couldn't remember renewing their insurance policy compared to those earning over £7,000.[91]

Over half of all outstanding mortgages are currently on fixed rates, as is more than 80% of all new lending, with the proportion of borrowers on variable mortgages standing at over a third.[92] [93] However, for the 14% of SVR payers who are on a low income this

[88] Davies, Finney and Hartfree, University of Bristol, Paying to be Poor, November 2016.
[89] Social Market Foundation, Measuring the Poverty Premium, March 2018.
[90] Those on low incomes often held mixed feelings about holding insurance, because they expected any claim to be rejected on the basis of a policy exclusion. Davies, Finney and Hartfree, University of Bristol, Paying to be Poor, November 2016.
[91] 11% of those earning under £7,000, compared to 3% of those earning £7,001 or over (base: 2,505).
[92] Analysis of Bank of England/NMG household survey data (2011-2017) of mortgage types, 62% of those who reported a mortgage type were on a fixed rate and 37% were on variable rate mortgages.
[93] Council of Mortgage Lenders, Are mortgage borrowers prepared for rising interest rates?, July 2017.

represents a much greater proportion of their household finances, particularly with the recent Bank of England interest rate rise.[94]

Level of education and the loyalty penalty

Evidence suggests that adults with degrees tend to perform better in complex tasks compared to those without.[95] It may be that people who did not go to university are less active in essential service markets because they have lower levels of confidence in dealing with complex processes and products. This is supported by the trends in knowledge reporting in our data. Those with lower levels of formal education are more likely than those with a higher educational background to express that they don't know whether new or existing customers pay more for the same service across all 5 markets tested.[96] And those who left education after secondary school are 7% more likely to say they have stayed loyal because they trust their current provider compared to those with university education.[97]

Lack of confidence may lead people to avoid engaging in the often complex process of switching provider. Across a range of essential markets, those who left formal education after secondary school are 3% more likely to pay the loyalty penalty than those with higher university degrees. And previous research by Citizens Advice found that those without a university degree are more likely to have done no shopping around before entering an essential service contract than those with a degree.[98]

[94] 14% of those who are over the fixed period of their 2, 3 or 5 year fixed rate mortgage are earning below £21,000. Base: 284.
[95] Tun, P. and Lachman, M., 'Age Differences in Reaction Time and Attention', Developmental Psychology, 2008.
[96] Analysis of responses of 3,030 British adults on whether they think new or long-standing customers pay more, less or the same on various essential services. In regards to home insurance, 26% of those who left formal education after secondary school responded that they did not know, compared to only 16% of those with a higher university degree.
[97] 48% of those who left education after secondary school stated that they trusted their provider across the five markets, in comparison to 41% of those with a university degree background or higher. Base: 625.
[98] Citizens Advice, The cost of loyalty: exploring how long-standing customers pay more for essential services, February 2018.

3. State of competition in essential markets

These markets - and we suspect other markets where consumers pay a loyalty penalty - are not working well for consumers. We believe it is unlikely that the problems behind this will be corrected by normal competitive forces.

The CMA's investigation into the energy market explained how weak consumer engagement was leading to adverse effects on competition. We think there is evidence that other essential service markets suffer from weak engagement and this could be leading to similarly poor outcomes. We also find evidence of market concentration and high profitability - two indicators, albeit imperfect ones, of competition not working well.

Due to the difficulty of examining competition problems without considerably higher access to company data, this is necessarily the most tentative of our chapters. All that has been feasible is to summarise features that may indicate further problems, rather than their definitive existence. We hope the CMA will examine these features in more detail and form a view about whether they indicate an underlying failing of competition.

This section sets out the current state of competition in the five markets we have studied, examining the similarities and differences with the energy market. It examines:

- Impact of consumer engagement on pricing
- Market concentration
- Profitability

For one thing, none of these markets are *'free'* in a traditional sense and one should expect competition to operate somewhat differently as a result.

Some, like broadband and mobile, are built atop a natural monopoly, where competition has only been enabled by careful market design (the privatisation of BT and the introduction of retail competition in the case of broadband; spectrum auction and regulation in the case of mobile). All are tightly regulated, in virtue of how essential they are to consumers and the often catastrophic consequences if these markets fail. Many have elements of price regulation already. And all have consumer inertia 'baked in' through long-lasting, automatically renewing contracts that allow price increases at the end of a contract. The opportunities for exploiting behavioural biases and inertia will be wider here than in other markets.

In its energy market investigation, the CMA found that consumers were paying £1.4bn more than they would have done in a well-functioning, competitive market. This revenue was largely collected from loyal customers of the six largest energy firms on a default standard variable tariff or on a prepayment tariff. The degree of disengagement

in the market was allowing large firms to make excessive profits off the backs of customer loyalty and reduced incentives for these companies to innovate and improve their efficiency, because they could rely on this unearned revenue from consumers.

While we cannot claim with confidence that similar dynamics can be found across essential markets, similar features - incumbency, dominance, reliance on loyalty, and high levels of profitability - are present. We do not have sufficient evidence to request that the CMA conduct a market investigation into whether any features of a market are preventing, restricting or distorting competition. Nevertheless, we think that through our proposed market study the CMA should collect further evidence regarding individual markets, and conduct a market investigation if the indications we report here show that there are adverse effects.

The impact of consumer engagement on pricing strategies

Every essential market we've studied, with the exception of mortgages, features low levels of engagement. This is relevant to competitive outcomes: the major reason that the CMA concluded there were adverse effects on competition present in the energy market was due to a lack of consumer engagement. The CMA identified:

> *"a combination of features of the markets for the domestic retail supply of gas and electricity in Great Britain that give rise to an Adverse Effect on Competition through an overarching feature of weak customer response, which in turn gives suppliers a position of unilateral market power concerning their inactive customer base."*[99]

Some firms argued that this was consistent with a competitive outcome: yes, they were charging loyal consumers a higher amount, but this was so that they could discount some non-standard tariffs, making them more attractive to new customers. They could only do this if a proportion of customers will revert to a standard variable tariff at the end of that tariff's term. Such a pricing approach might be distributionally unfair, but still could lead to the excess paid by loyal consumers funding cheaper deals for more engaged consumers.

However, the CMA instead found that *average* prices were higher than would occur in a well-functioning competitive market. In a similar vein, they found that energy suppliers' acquisition tariffs track changes in underlying costs much more quickly and accurately than their standard tariffs.[100]

They concluded that there were significant disparities in the tariffs charged by the six largest energy companies that could not be fully explained by differences in cost and that it was a lack of customer engagement that gave these firms the power to raise prices for those customers.

[99] CMA, Energy market investigation: Final report, June 2016.
[100] CMA, Energy market investigation: Final report, June 2016.

Could the same effect be happening in other markets? Outside of energy, time-series data on levels of switching over time is not readily available. And each market exhibits different optimal frequencies of switching, depending on the normal initial length of contract and other market characteristics. This makes it difficult to directly compare switching rates across markets.

Nonetheless, a number of markets feature a weak customer response:

Table 4: Switching in essential markets

Market	**% of consumers who have not recently switched**
Mortgages	**23%** of consumers do not switch to a new mortgage deal within 6 months of moving onto a reversion rate.[101]
Mobile Handset	**36%** of mobile handset consumers did not switch after their minimum contract period ended.[102]
Broadband	**39%** of dual-play customers did not switch after their initial contract period expired.[103]
Insurance	In 2015, **72%** of combined home insurance customers at one insurer did not shop around at their most recent renewal.[104] Switching rates have remained static since then.[105]
Savings	**80%** of easy access accounts have not switched in the last 3 years.[106]

Across all markets represented, long-standing customers pay more than new customers - but in most markets, a significant proportion of customers remain disengaged. The main exception to this is the mortgage market, where switching rates are very high (which is to be expected, given this is many households' biggest expense). It therefore seems unlikely that any adverse effects on competition are caused by low customer engagement in this market.[107]

[101] FCA, Mortgages Market Study, May 2018.
[102] Citizens Advice, Mobile phone networks overcharging loyal customers by up to £38 a month, October 2017.
[103] Ofcom, Pricing trends for communications services in the UK, May 2018
[104] FCA, Encouraging consumers to act at renewal, December 2015. Survey question: At the time of your most recent motor/home insurance renewal, did you search around for alternative insurance policies e.g. searched online or phone insurers for quotations?
[105] FCA, Sector Views 2018.
[106] FCA, Cash Savings Market Study, January 2015.
[107] However, as described in Chapter 3, those paying it are still particularly likely to be vulnerable.

Just under 3 in 4 home insurance customers have remained loyal to their provider at renewal, without searching around for other quotations.[108] However, in 2017, the FCA observed that '*[insurance] providers have tried to increase profitability by...introducing dual pricing*'.[109] So rather than competing through innovation or low prices, insurance providers are charging different prices to loyal customers for the same product.

Consistent with this, the FCA found that home insurance premium increases are consistent with a 'shrouded equilibrium' model,[110] where consumers do not anticipate they will purchase additional products at high prices (in this case, more expensive home insurance) when they purchase the original product.

Meanwhile, the extremely low switching rates in the savings account market, despite a range of interest rates on offer, suggests that competitive forces are not producing the expected effect in this market. This was clearly reflected by the FCA in their market study, where they found that competition in this market is not working effectively for many consumers. The FCA has also published a discussion paper on introducing a basic savings rate after concluding that the information-based remedies trialled would not address the underlying flaws in the market.[111]

In the broadband market, the average household spend has risen in recent years, primarily due to the growing prevalence of superfast broadband.[112] According to Ofcom, the growing complexity and availability of tariffs could lead consumers to disengage from the market entirely. Indeed, considering the size of the loyalty penalty, this market features a very low engagement rate (as measured by switching levels). This complexity and disengagement could be leading to adverse effects on competition.

While the CMA and EC have found the mobile handset market to be competitive, the market still has the characteristic of weak customer response to price. The structure of handset-inclusive contracts currently makes it very difficult for consumers to make informed purchase decisions on the basis of price. And, in addition to the penalty paid by long-standing customers, Ofcom recently found that those who purchase a package of mobile handset and service together pay a premium of up to 34%.[113]

The increasing sophistication of algorithms and segmentation means providers will be able to accurately target people who are likely to be loyal, or likely to switch, with prices to match.[114] So the trends identified here may only grow.

[108] Citizens Advice analysis of ComRes data on "When did you begin your current contract for each of the following services?: Home Insurance". Base: 2,952.
[109] FCA, Sector Views 2017.
[110] FCA, Occasional Paper 12, December 2015. Data from three home insurance companies, not market wide.
[111] FCA, DP18/6: Price discrimination in the cash savings market, July 2018.
[112] Ofcom, Pricing trends for communications services in the UK, May 2018.
[113] Ofcom, Pricing trends for communications services in the UK, May 2018.
[114] Citizens Advice, A Price of One's Own: An investigation into personalised pricing in essential markets, August 2018.

Collectively, this indicates that some companies may have the power to raise prices for unengaged consumers in a way that need not benefit other consumers. The CMA should investigate whether the weak customer response in these markets is having an adverse effect on competition; and, more generally, whether it is the case that the loyalty penalty should be expected to lead to worse competitive outcomes wherever it exists.

Market concentration

Market concentration can also be an indicator, albeit an imperfect one, of competitive intensity. While highly concentrated markets can be competitive, high levels of concentration can indicate competition is not working well (though do not in themselves *explain* why competition is not working well).

Across essential markets, a small number of providers tend to hold a large proportion of the overall market share.[115] These providers tend to dominate where services have previously operated under monopolies, such as telecoms and energy services, though the market share of incumbent suppliers is declining. The main exception to this is the insurance market, where the largest providers have a noticeably smaller proportion of the market.

Table 5: Concentration in essential markets

Market	Dominant providers	% market share
Broadband	5	91%[116]
Mobile (including handset)	4	86%[117]
Energy	6	77%[118]
Savings	6	68%[119]
Mortgages	6	75%[120]
Home Insurance	5	45%[121]

[115] See Appendix for more details. Each of the six markets explored in this research have Herfindal-Herschman Index scores of 1,000 or more which mean that they can be classified as 'concentrated', according to SMF, Concentration not competition: the state of UK consumer markets, 2017.
[116] Ofcom, The Communications Market Report, 2016. This is the share of residential and SME broadband services. The providers are Virgin Media, EE, BT, TalkTalk and Sky.
[117] Ofcom, The Communications Market Report, 2016. This is share of retail mobile subscriptions. The providers are Vodafone, O2, EE and Three.
[118] Ofgem, Electricity supply market shares by company, 2017. The providers are British Gas, E.On, EDF, npower, Scottish Power and SSE.
[119] FCA, Cash savings market study: final findings, January 2015.
[120] FCA, Mortgage Market Study: Interim report, May 2018. The providers are Barclays, Lloyds, RBS, Nationwide, Santander and HSBC. FCA report states 'around three quarters' & the market shares are for balances of outstanding first-charge residential mortgages.
[121] IBISWorld, *Home insurance industry report*. The providers are AXA, Aviva, Direct Line, Lloyds and Royal and Sun Alliance. Refers to domestic property insurers only.

The Social Market Foundation found similar results, with eight out of ten consumer markets they studied described as 'concentrated'.[122]

These dominant providers tend to have large proportions of long-standing, or 'back-book', customers. For example, the FCA found that in 2013, 17% of large providers' cash ISA balances were held in accounts opened more than 5 years ago, compared to 5% for small and medium banks.[123]

This dynamic enables large providers to maintain dominance in the market without necessarily competing on price. In their cash savings market study, the FCA found that large current account providers have a considerable market advantage, because they could attract the most easy access balances despite offering lower interest rates. As a result, while there are over 100 providers in the savings market, over two-thirds of the market is controlled by just 6 providers.[124]

Profitability

Firms making super-normal profits over the short-run - that is, profits over and above their costs and their necessary investor return - can be consistent with competitive market outcomes. But sustained high levels of profit across industries can be an indicator of markets that are not functioning well. In its energy market study, for example, the CMA estimated that customers with the largest six energy providers were paying, on average, £1.4bn more each year (over the period 2012 to 2015) than they should have been under a well functioning market. Of this, £650m a year (from 2012 to 2014) was due to excess profits.[125]

Many other essential markets experience persistently high levels of profit, that could indicate that competition is not working well in these markets. Table 6 shows the annual profitability of the largest providers in each of the five essential markets we have identified a loyalty penalty, over the past five years. The full figures are included in Data Appendix 2.

Table 6: Profitability in essential markets

Market	Total profits of largest providers
Broadband[126]	£3.1bn
Mobile (including handset)[127]	£5.2bn

[122] Social Market Foundation, Concentration not competition: the state of UK consumer markets, 2017.
[123] FCA, Cash Savings Market Study, January 2015.
[124] FCA, Cash Savings Market Study, January 2015.
[125] CMA, Modernising the Energy Market, 2016.
[126] Citizens Advice analysis of InFront Analytics & Companies House results; average annual net operating profits of BT (including EE), Virgin, TalkTalk and Sky.
[127] Average annual net operating profits of EE, O2, Vodafone and Three.

Retail finance (savings and mortgages)[128]	£12.3bn
Insurance[129]	£7.9bn
Total[130]	£25.3bn

There are limits to this analysis: often these profits relate to multiple different products that that firm provides, rather than just the markets we refer to. And we do not reach a conclusion on what profit is necessary to deliver investment and ensure competition in these markets. However, these sectors seem healthily profitable, suggesting that companies could reduce the prices that they charge loyal customers. The high levels of profit indicate that there could be problems with how competition is working in these markets.

There is also evidence that in some cases, a disproportionate level of firms' profits come from loyal customers. For example, the CMA market investigation found that across the Big Six energy suppliers, average revenue from customers on the standard variable tariff (SVT) was around 11% and 15% higher than average revenue from fixed electricity and gas tariffs.[131] And the FCA's investigation into the home insurance market found that, for the firm it was able to investigate, while revenue from customers who had renewed their policy over 5 years was 70% higher than that acquired from a new customer, this was not matched by an increased likelihood of a claim being made, so the cost of serving that customer was unchanged.[132]

When a large portion of firms' profits come from loyal customers sitting on poor value deals, the competitive pressures companies face are undermined. By raising prices for loyal customers, incumbents are able to tempt in new business with artificially low prices without innovating, competing or sacrificing their profit margin. These low prices also make it difficult for new entrants to gain a foothold in the market, helping incumbents retain large market shares.

The effects on competition

Concentrated, often marked by incumbency, weak consumer engagement and high profits: many of the markets where the loyalty penalty exists are near textbook definitions of markets where competition is not working well. Given the similarities to the energy market, they often seem strong candidates for features that cause adverse

[128] Average annual net operating profits of Barclays, Nationwide, HSBC, RBS, Santander and Lloyds.
[129] Average annual net operating profits of Axa, DirectLine Group, Lloyds, Royal and Sun Alliance and Aviva.
[130] Does not sum, as Lloyds is present in both the insurance & retail finance markets and BT is present in both mobile & broadband markets.
[131] CMA, Energy Market Investigation, February 2016.
[132] FCA, Encouraging insurance customers to act at renewal, December 2015.

effects on competition. We aim to be cautious in stating what can be claimed at this stage. But at the very least, these features merit careful further study by the CMA.

4. The record of previous interventions

In the past 15 years, regulators, Government and consumer bodies have tried to improve consumer decision-making, increase switching and reduce switching costs. These efforts have often led to modest improvements in switching. But they have not been proportionate to the size of the problem - and have not fixed the problem.

This section sets out the successes and failures of previous regulatory interventions. It finds that while demand-side regulation has sometimes had positive impacts, and its regulatory design and testing has improved over time, it has not led to significant market changes.

The limited effects of prior reform

Prior reform has largely focused on disclosure remedies: making sure that consumers are aware of their ability to switch and the likelihood of price rises if they remain with their existing provider. More sophisticated versions of these remedies have tested different methods of providing this information to elicit the highest response possible.

Table 7: Effect of measurable switching remedies

Market	Intervention Description	Effect on switching
Energy[133]	Ofgem requires that energy companies provide a cheaper tariff message on all bills since late 2013.	Previous tracking surveys have indicated that some consumers took some form of action by switching tariff or supplier in response to these prompts on their bills. No ongoing evidence is available about how this translated to increased switching or increased value for money.
Cash ISAs[134]	The OFT secured agreement from banks to show interest rates on ISA statements in 2010. Following a further market study, the FCA put in place new rules requiring that these be placed prominently.	The OFT's review of the original intervention found that awareness of interest rates **lowered** during this period (plausibly because the Bank of England interest rate was lowered over the same time period).

[133] Professor Amelia Fletcher, The role of demand side remedies in driving effective competition: A Review for Which?, November 2016.
[134] Professor Amelia Fletcher, The role of demand side remedies in driving effective competition: A Review for Which?, November 2016.

Savings[135]	Cash savings disclosure remedies This trial tested the effectiveness of three different types of information provision interventions: ● Information about comparable higher-rate-paying products ● A pre-filled return form that enabled simplified switching ● A reminder about the rate decrease	Overall, all the interventions increased switching within internal providers, but not to higher-paying products from other firms. ● Front-page information about available higher rates led to an increase in switching from **3% to 6%** of consumers. Non-front-page disclosures had **no effect**. ● A pre-filled return form increased switching from a baseline of **3% to 12%**. ● Optimal timing of reminders to switch prompted an increase in switching from **4.7% to 8.2%**.
Home and motor insurance[136]	Encouraging customers to act at renewal This trial measured the impact of different types of renewal notices for customers switching/negotiating their insurance policy at renewal. It tested four types of disclosures: ● Including last year's premium next to this year's premium in renewal notices ● Sending a leaflet with renewal notices e.g. a guide to shopping around ● Simplifying renewal notices by using bullet points and simpler language ● Sending reminders two weeks after renewal notices	Putting the previous year's premium on renewal notices caused a **3.2%** increase in consumers switching or negotiating their home insurance policy. There was little evidence of price increases at renewal found for customers at the two motor insurers, and including last year's premium has **no effect**. Other changes to renewal notices, such as simplifying them, sending information leaflets and reminders had **little or no impact** on consumer behaviour.
Current accounts	The Current Account Switching Service (CASS) was launched to reduce frictions switching for Personal Current Accounts,	Switching rates in 2017 increased to **1.8%** a year.[138]

[135] FCA, Attention, Search and Switching: Evidence on Mandated Disclosure from the Savings Market, July 2016.
[136] Financial Conduct Authority, Occasional Paper No.12 Encouraging consumers to act at renewal: Evidence from field trials in the home and motor insurance markets, December 2015. Data from three home insurance companies, not market wide.

	Charities and Business Current Accounts.[137] The Current Account Switch Guarantee now ensures that banks take care of closing the old account, moving balances and switching payments.	
Energy[139]	Cheaper Market Offers Letter trial. Randomly allocated 150,000 default tariff customers to receive either: ● No letter (control group) ● An Ofgem-branded letter showing personalised cheaper deals from rival suppliers ● A supplier-branded letter showing personalised cheaper deals from rival suppliers The test observed the switching rates for each group for thirty days after the letters were sent.	Letters increased switching from a baseline of **1%** to an **average of 2.9%**.
Energy[140]	CMA database remedy Tested 2,400 customers who had been on a default tariff for 3+ years, and randomly allocated them to receive either: ● No letter (control group) ● An Ofgem-branded letter showing personalised cheaper deals (best offer letter) ● Up to six marketing letters from rival suppliers (simulating the CMA remedy)	*Customers were sent a letter from their supplier advising them that they could opt out of being sent energy deal offers. After 28 days, those who didn't opt out then received either the cheaper deals letter or marketing material.* The CMA database remedy resulted in switching from **6.8% to 13.4%** (CMA remedy) or **12.1%** (Ofgem best offer letter).
Energy[141]	Active choice collective switch trial	**22.4%** of customers in the trial

[138] 931,956 switches were conducted in 2017, compared to an estimated number of banked adults of 50.6m. ONS number of adults. 1.5m (number of unbanked adults). Source: BACS, Current Account Switch Service Dashboard, 2018; Financial Inclusion Commission.
[137] Behavioural Insights Team for Citizens Advice, 'Applying behavioural insights to regulated markets', May 2016.
[139] The Behavioural Insights Team, One letter that triples switching, February 2018.
[140] Ofgem, Small Scale Database trial, November 2017.
[141] Ofgem, Open letter: Active choice collective switch trial - early findings, August 2018.

	Using the disengaged customer database, Ofgem identified 50,000 customers who had been on the same deal for 3 years or more. Consumers could opt into a collective switch run by a price comparison website (PCW), as well as opt out of further communication. The following data was all shared with the PCW running the collective switch: name, address, current tariff and historic consumption data. All of this data was shared without consumers' consent.	switched overall, compared to a baseline of 2.6% in the control group. Customers who switched saved around £300. Vulnerable consumers were as likely to switch as the remainder of the intervention group.

These interventions are often better designed than they were a decade ago, as regulators have become more informed regarding behavioural nudges and randomised controlled trials to evaluates the effectiveness of interventions.

Until very recently, even the most promising study here offers a maximum increase of 8-9% in switching during the trial period. This accords with expert views. Professor Amelia Fletcher, in her review of the efficacy of demand-side remedies, found that:

> *'a number of demand-side remedies, of various sorts, have had beneficial effects. However, many have not been as effective as intended, and a few may even have had unintended negative consequences'.*[142]

Martin Cave, incoming Chair of Ofgem and former CMA Panel Member, in reference to the energy market, concluded that:[143]

> *'we have seen a variety of measures, covering such things as bill formats and customer prompts, barrages of publicity adverse to energy companies...and very large amounts of column inches, TV advertising and other advice devoted to explaining how to switch supplier. Yet none of these developments has made a dent in the proportion of customers of the six large energy firms.'*[144]

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[142] Professor Amelia Fletcher, The Role of Demand-Side Remedies in Driving Effective Competition: A Review for Which, November 2016.
[143] Martin Cave, Written evidence from Professor Martin Cave OBE to the Business, Energy and Industrial Strategy Committee, November 2017.
[144] Recent market data suggests that the Big Six's market share has declined by roughly 10% in the two years since the CMA's final retail energy market report. Ofgem: Electricity supply market shares by company: Domestic (GB), Gas supply market shares by company: Domestic (GB).

However, the publication in August of early trial results of Ofgem's collective switch trial shows a (comparatively) large increase in numbers of consumers switching. While these are preliminary results, and Ofgem will be extending these trials to see if the level of switching holds up, collective switching seems to be leading to encouraging results that could reduce bills for a significant fraction of consumers. As discussed in our conclusions section, we think (while there are data protection and consent issues to consider) this represents the most promising approach in getting more consumers to engage.

Our previous research shows why most reforms have failed

By treating this problem as one which consumers can solve through increased switching and 'better' decision-making, the regulatory approach has often ignored the complexity and difficulty many consumers face when switching. In markets where the costs (potential or actual) of switching are high, demand-side remedies can only go so far.

Switching in these essential markets is rarely a frictionless experience. It is difficult for many consumers, it often has costs that are perceived to outweigh the potential benefits and it is not always a priority for people with time-poor lives (especially given the amount of time necessary to make a good decision).

Previous research from Citizens Advice has found that the following factors have limited the effectiveness of demand-side remedies:

1. People don't have the time to shop around anymore
2. Finding a good deal is a struggle
3. Vulnerable consumers are often unable to access the best deals
4. The financial cost of switching is often prohibitively high
5. Fear of things going wrong puts people off taking action

1. People don't have time to shop around anymore

Even simply recognising higher bills relies on consumers reading and understanding their bills on a regular basis. But evidence gathered from the Citizens Advice network and consumer service shows that many people are surprised by tariff rises, or never notice them at all. Previous research by Citizens Advice has found that vulnerable consumers are particularly unlikely to do so.

Recent regulation has focused on the time it takes to switch from one supplier to another. But the length of time it takes to decide whether and where to switch is likely to be at least as important as how long the switch itself takes.[145] The focus assumes that shopping around more is always a positive thing. In fact, the research shows consumers feel less satisfied when they spend a 'good' amount of time reaching a decision.[146]

[145] The Behavioural Insights Team, Behavioural Insights Team response to Energy market investigation: Notice of possible remedies, November 2015.
[146] Citizens Advice, 'Against the clock', November 2016.

Consumers who shop around will always be central to a well-functioning market. But people lead complex, busy lives, often juggling work and caring commitments and making a huge number of choices each day. In order to make well-informed decisions in essential service markets, consumers would need to almost double the amount of time they spend shopping around.[147] But even among those who would like to spend more time shopping around for essential services, only 1 in 6 say they have the time (16% of consumers overall).

2. Finding a good deal is a struggle

Previous Citizens Advice research has found that many people find the process of finding a good deal prohibitively difficult.[148] In addition, research by Citizens Advice finds:

- 18% of respondents cited 'the process was difficult' as a reason for staying in at least one essential service contract.
- A third (35%) of respondents think it is not straightforward to find a good deal in essential service markets.
- 1 in 5 respondents selected at least one negative reason for remaining on their energy, broadband or mobile handset contract.[149]

Behavioural insights can help explain the limitations on people's ability to shop around. The way choices are designed can have a big impact on consumer behaviour, even when the economic incentives for a consumer are clear. Providers of essential services exploit this to charge steep prices to long-standing customers:

- **Inertia/status quo bias** describes people's tendency to stick with a previous decision or the default despite there being benefits from switching. Particularly in the face of complexity, or 'choice overload', people either resort to inaccurate 'rules of thumb', or they stick with the default option. Inertia is one of the strongest forces in consumer behaviour.
- **Overconfidence and optimism** lead people to overestimate their abilities and knowledge. Optimism leads people to overestimate the likelihood of a positive outcome and underestimate that of a negative one. For example, consumers also tend to overestimate their ability to regularly pay off loans.
- **Temporal effects** mean that while reminders are powerful, timing is crucial. Studies have found that individuals save more if reminded to at timely moments. A recent study found that very high savings anchors were not very effective unless sent when people had just received bonuses. People are also more likely to act at the start of a new month or year, or on a meaningful date.

3. Many vulnerable consumers are unable to benefit from the best deals

There are also specific circumstances in which it is difficult for customers to switch. Customers in debt can, counter-intuitively, be forced to stay on significantly higher cost

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147 Citizens Advice, 'Against the clock', November 2016.
148 Citizens Advice, 'The Future of Digital Comparison Tools', May 2017.
149 Negative reasons were 'The process was time consuming', 'The process was difficult' or 'I had to pay a fee to exit the contract'.

tariffs due to an inability to switch:

Case study:

Gregoire came to Citizens Advice when he started struggling financially. He has a contract for TV, broadband and internet with his provider, but is now outside of the initial 12 month contract. He can't afford the new monthly contract costs, however, and has fallen into arrears. Gregoire has tried to cancel or reduce his monthly package but was told by his supplier that he can't make changes whilst he is in arrears. His debt is continuing to increase because he can't afford to catch up sufficiently to cancel his contract, and find a better deal.

People who don't have internet access also find it more difficult to switch. Lack of internet access can make it challenging for consumers to make use of comparison websites, and easily access a variety of information to make informed choices. It can also exclude consumers from the best deals, as these often require having an online account or email address. As the previous section demonstrated, people who aren't digitally literate or don't have access to the internet can often be more vulnerable consumers. These groups would often benefit the most from being able to switch easily.

Case study:

Klara, 80, came to Citizens Advice because she was struggling to pay her service charge on her home and manage financially. She has been scrimping and saving to pay her bills and get by without falling into debt with her insurance and energy providers. She can't use a computer, and therefore is unable to research information online that would show the benefits of switching. As a result, her outgoings are higher than they could be. Klara was not aware of the savings she could make, as she believed there was a benefit to be had from loyalty to her suppliers. Lacking computer literacy, Klara hasn't got the best value for money and feels foolish for going without to pay her bills.

Customers who favour or require particular payment methods also face obstacles in the actual process of switching, or accessing the benefits of switching.

Case study:

Emem came to Citizens advice after he'd switched to a new provider for his internet and phone service. This had seemed like a good deal, and he had believed that he would be paying just over £20 per month. When he made this decision, his providers had not explained that he would be charged quarterly, and a larger direct debit of £80 was drawn from his account a few weeks later. This payment plan didn't work for Emem, and he therefore had to cancel his contract. Due to the inflexibility of the provider, Emem hasn't been able to benefit from a good deal with his preferred payment plan. He's missing out on savings because he needs a deal which he can pay for monthly, which might not work out as the cheapest available.

4. The financial cost of switching is often prohibitively high

Sometimes people's problems with switching have resulted in a financial cost, making it impossible for them to avoid a penalty for either switching or remaining loyal. Others incur ongoing loyalty costs because they are unable to switch. Analysis of a sample of local Citizens Advice cases found our clients faced a median cost of £240 from problems caused by switching. In the broadband market, the median cost is higher, at £275.[150]

Case study:

Youssef, 65, has health issues which mean it's vital that he has a working phone. He switched to a new landline provider at the end of May, and was assured that it would be up and running in the first week of June. Despite multiple calls to his new provider, it still wasn't working by the end of June. Youssef decided to switch back to his old provider as the new one had failed to deliver its promised service, and he hadn't signed any contracts. His new provider got in touch and told him that he owed £230 for cancelling the contract. Youssef is not interested in modern technology and feels vulnerable and annoyed that the new provider broke their promises and are now demanding a payment he wasn't aware of.

Exit fees, even when they only relate to the minimum contract period, can add to the perception that it's difficult to switch. Exit fees for exiting a contract early have also risen dramatically in the telecoms market, with consumers paying 50% more to exit contracts early than they were in 2010.[151] Evidence from the Citizens Advice consumer helpline also raises concerns about the circumstances in which these fees are charged, including:

- Charging exit fees even when consumers have been experiencing persistent service faults.
- Applying the same level of exit fees to consumers who are in their second or subsequent contract with the provider, despite not needing to recover installation and initiation costs.

Case study:

Georgia was phoned by her broadband and TV provider, offering her free movies as a loyal customer. She took the initial offer but was surprised seven months later that her monthly bill had gone up by £17 a month. It turned out that the movies were only free for a six month period and she was now being charged. Georgia found it difficult to remove the movies and eventually decided to leave her provider, who she had with for seven years. When she asked to leave she was told that she would be charged an

[150] Calculated through analysis of 74 Evidence Forms submitted by local offices which mention a specific cost related to switching or tariff changes across all essential services (broadband, mobile, insurance, mortgages and banking). Refer to Appendix B for full details.
[151] Citizens Advice, Broadband exit fees, March 2018.

exit fee of £240, because in accepting the movies she had entered into a new 18 month contract.

5. Fear of things going wrong puts people off switching

When people do invest time in shopping around to get a good deal, they can often come upon further obstacles when they are trying to make a switch. Research by Ofcom found that a quarter of those who switch mobile provider had experienced major difficulties with the process. These difficulties also affected 37% of consumers who had considered switching but did not do so.[152] And nearly 1 in 4 (23%) of all broadband-related problems recorded by the Citizens Advice consumer helpline involved difficulties cancelling and/or switching provider.[153] Many of these obstacles are unnecessary, and stem from supplier-side issues that can be avoided or easily fixed.

Fear, or experience, of switches going wrong can put consumers off in future. This is not necessarily an irrational fear: for many vulnerable and low income consumers, the impact of something going wrong can be considerably worse than for the average consumer. This in turn can cause financial problems when consumers remain in a contract that is not suitable for them.

Case study:

Sameera is elderly and disabled, as well as being a carer for her husband who has cancer. They are on a low income and receive pension credit and a carer's allowance. Sameera wanted to switch her landline provider in order to save some money. She phoned up to sign up to a new deal, and during the phone call felt pressured into agreeing to get a bundled contract including broadband and a mobile sim-only contract, in spite of not owning a mobile or computer. Sameera now faces increased costs, but is too worried about the process of switching to try again. She therefore sought advice from Citizens Advice.

Collectively, these five factors help explain why people do not switch and why even the best designed remedies often do not succeed.

[152] Ofcom, Consumer Switching: Decision on reforming the switching of mobile communication services, December 2017.
[153] Citizens Advice, Cancellation fees "punishment" for switching broadband suppliers, August 2014.

5. Conclusions

The loyalty penalty is a persistent and - for those who pay it - punishing feature of many markets. Prior attempts to fix it have not succeeded. This is largely because they have rested on assumptions that customers would react in a way that it is not reasonable to expect them to. As a result, there remains a large loyalty penalty - disproportionately paid by the most vulnerable in society and affecting the poorest proportionately the most.

Competition has delivered real benefits for some consumers in terms of cost and better quality of service, but it is not working for all of them. Attempts to remedy the situation that place all the responsibility in consumers' hands have not worked - either because these consumers cannot get on to the best deals or because they face significant barriers in doing so.

In certain markets, we have concrete recommendations regarding solutions. In the mobile market, where the rip-off is most blatant, we think the practice of continuing to charge for the handset after the minimum contract term must come to an end. We therefore welcome Ofcom's consultation on how it can end this practice by introducing fairer default tariffs.[154] In others, there may be ways of strengthening existing proposals - examining whether a relative cap on mortgages might reduce detriment in the mortgage market[155] or the merits of strengthening a Basic Savings Rate by (for example) linking it to the Bank of England rate.

However, more generally, we do not propose a comprehensive vision of how this can be fixed: this is a task that the CMA will be best placed to undertake, through conducting an investigation during the 90 day super-complaint period and the consequent market study we expect will be necessary. We have included our past policy recommendations as Appendix F, but we think these represent the beginnings of a solution rather than its end.

We think solutions will fall into three types and some combination of the following interventions will likely be successful. The CMA's market study should consider:

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

[154] Ofcom, Helping consumers to get better deals in communications markets: mobile handsets, September 2018.
[155] Citizens Advice, Improving the Mortgage Market, Citizens Advice formal FCA Mortgage Market Study response, August 2018.

The remainder of this section discusses potential remedies in each category. It is not intended to be exhaustive: ultimately, through the market study we propose as a consequence of this super-complaint, the CMA will identify and evaluate these and other solutions.

Engaging more consumers in these markets

Two approaches are likely to improve consumer outcomes here. One is ensuring that the disclosure remedies that have emerged from randomised controlled trials as the most successful way of eliciting customer switching are implemented by regulators across markets (subject to individual market circumstances and a judgement regarding the generalisability of findings to other markets). There is a considerable gap between the worst and best performing remedies, so getting this right will help some customers get a better deal.

A second approach is indicated by Ofgem's Active Choice Collective Switch Trial, discussed above. If this can be replicated, there is a possible argument for extending it to other markets where it is possible to design collective switching schemes.

This relies on regulatory access to customer data and that data being shared with trusted third parties. There are consequently serious potential risks to consumer trust in the market and many consumers may be uncomfortable with their data being shared without their consent. Any credible approach would need to be designed to share the least data necessary for better consumer outcomes, with clear opt-out opportunities.

Even if this challenge can be surmounted, we would caution against seeing it as a panacea. Energy benefits from relative product simplicity, making it a good choice for designing a collective switching remedy. Such an approach may prove less tractable in markets where consumers must make a greater number of decisions at the point of switching. However, it still merits further investigation and study.

Direct interventions into these markets to minimise the loyalty penalty

However successful the above approaches prove, unless all consumers switch, they will not solve the underlying market structure. Some fraction of consumers will always be paying a penalty. Even in the most promising study so far, using the most interventionist demand-side approach feasible, 78% of all customers still did not switch to a better energy deal and 78% of customers on the Priority Services Register remained on poor deals. These consumers deserve protection - the CMA should therefore examine the case for intervening directly into what suppliers are able to charge loyal customers. A number of approaches may be feasible in this regard.

A price cap has been introduced into the energy market to restrict the loyalty penalty paid by consumers. But we think such a price cap is unlikely to be feasible in other markets: setting a price for a homogenous good such as energy that is indexed to observable costs is challenge enough for Ofgem. For products with great diversity and

complexity, the challenge for a regulator is considerable and the risk of negative unintended consequences much higher. While we think the CMA should review the practicality of these approaches, we think it is unlikely that it is feasible in other markets.

A second option is a price differential cap. This limits the difference charged by a supplier between its best and worst deals. A similar measure is being considered by the FCA in the cash savings market, which would ensure that all easy access cash savings providers offer customers not on an initial deal the same Basic Savings Rate. As we have argued in relation to the FCA's Mortgage Market Study, there is reason to think that a relative restriction between introductory and standard rates for mortgage consumers might lead to lower prices for consumers on standard variable tariffs rather than an increase in introductory rates.

A third option is to introduce principles-based regulation regarding what pricing strategies are permissible, putting the responsibility on companies to judge whether their practices are consistent with treating customers fairly. This would enable regulators to allow for an evolution of competition over time, recognising that many of these markets are fast-changing and that pricing practices may need to change rapidly as a result. However, it would also allow regulators to clamp down on excessive price differences or ripping off consumers over a long period of time.

The risks associated with demand-side responses are limited; this is why regulators have traditionally preferred them. We recognise that direct price regulation can carry significant risks to the competitive dynamics in the market, so must be carefully considered. In certain circumstances, price discrimination can intensify competition[156] and there are examples of well-intentioned attempts to regulate price differentials in the UK that have failed.[157]

Nonetheless, we think it is likely that skilful interventions can be found that properly balance between reducing price differentials for loyal consumers while also ensuring that competitive dynamics are not disrupted. The FCA has been pioneering in this approach, using price regulation as an active part of its regulatory arsenal. In designing a remedy package, the CMA should examine where approaches like these can be deepened and extended.

Specific protections for vulnerable and low income consumers

Significant price differentials for loyal consumers are unfair no matter who they hit - no other markets require this peculiar and difficult kind of engagement from consumers

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[156] Tariff diversity *may* have led to greater broadband adoption in the EU, for example. Mirjam R.J. Lange, Tariff Diversity and Competition Policy — Drivers for broadband adoption in the European Union, July 2017.
[157] For example, limits on how much energy companies could charge their pre-privatisation region's customers led to many suppliers increasing prices for acquisition deals, rather than lowering everyone's prices. Waddams Price and Zhu, Pricing in the UK retail energy market, 2005 - 2013, December 2013.

every 1-2 years in order not to get ripped off. But these penalties proportionately hit the poorest and most vulnerable in society's budgets the most. Well designed markets should serve not punish these groups. In devising what remedies are appropriate, and in thinking about making any potential trade-offs in designing these remedies, the interests of these groups should be prioritised. This consideration does not necessarily require targeted solutions (well designed whole of market interventions may also particularly protect these sections of society). However, in certain circumstances, remedies that might not be appropriate for the whole of the market may be justifiable for certain consumer groups in service of this prioritisation.

There will always be consumers who can't, by themselves, engage with these markets, but who rely on the services. This protection might include tariffs or contracts specifically designed to ensure that those defined as vulnerable, and unable to engage in the markets, are not exploited. We expect this could include:

- Any of the interventions into companies' prices for loyal consumers could work for a more targeted set of consumers.
- Automatically putting all vulnerable consumers on the best deal available.
- Prioritisation of vulnerable consumers for collective switching programmes.
- Trialling of new digital tools with vulnerable consumers.

These solutions are not without challenges. Defining who should be protected is not simple. There will be groups of consumers who will never be able to engage in the market and there will be others who might not be able to engage temporarily. However, while defining vulnerability perfectly is analytically challenging, a practical definition for the purposes of price protection need not be - simply identifying certain demographic cohorts who are likely to be vulnerable or in need of protection should be sufficient.

Identifying vulnerable consumers is also challenging. Self-reporting is not sufficient as these consumers are already dis-engaged with the market and are therefore unlikely to respond to any requests for information. Voluntary take up of support in other areas (such as welfare benefits) is typically not universal. To navigate the identification challenge, new data-sharing powers from Government may well be needed.

Ultimately, there will not be a silver bullet to solving this problem across markets and the CMA will need to design a comprehensive package of reforms. We look forward to working closely with it during the investigation period.

Appendix A: Size and scale of the loyalty penalty

Quantifying the number of people paying the loyalty penalty

The data used in this super-complaint is based on several years of research into the loyalty penalty from Citizens Advice. We have used a combination of this prior research alongside more recent polling and data analysis for our methodology. Additional appendices are attached detailing our data in full.

We commissioned Populus and ComRes to carry out three sets of polling of 2,000-3,000 people to identify how many people pay the loyalty penalty and the markets where it's most common. This polling also looked at attitudes towards and behaviours associated with the loyalty penalty in essential markets. We performed an analysis of the survey results weighted to be demographically representative, which are attached in Data Appendix 1 as Excel files.

Analysis of ComRes polling of 3,030 people in R software identified how many people are currently paying a loyalty penalty in each of the essential markets this complaint focuses on.

Table A1: Number of survey respondents paying loyalty penalty[158]

Market	Number of respondents[159]	Number of people paying loyalty penalty	% of people paying loyalty penalty[160]
Mobile (including handset)	3,003	1,009[161]	34%
Broadband	2,967	1,268[162]	43%

[158] Full results in Data Appendix 1.
[159] 3,030 respondents.
[160] Based on all survey respondents, not only respondents who have a contract in the market.
[161] Anyone with contract for more than 2 years.
[162] Anyone with contract for more than 3 years.

Home Insurance	2,952	1,379[163]	47%
Savings	2,973	1,095[164]	37%

People were classed as paying the loyalty penalty based on how long they had been with their current provider in each market. The base for each market is all survey respondents. A Citizens Advice researcher attempted to find the longest fixed-term contract available in each of the markets assessed in this super-complaint. Where many different contract lengths were available, the longest period was chosen, even if many providers only offer shorter length contracts.

This is a conservative approach to estimating the scale of the penalty. Some people will have taken out contracts that are shorter than the maximum available in a particular market, and will subsequently have defaulted onto a poor value deal. These people are not identified by this report's calculations.

Table A2: Parameters of the loyalty penalty by market

Market[165]	**Maximum contract length (years)**	**Details**
Mobile (including handset)	2	Regulatory requirement under the EU telecoms package: no consumer contracts can be more than 24 months.[166]
Broadband	3	Longest basic broadband contract length found was 2 years. However, to ensure a conservative estimate, 3 years has been used as the penalty parameter.
Home insurance	1	Searched for quotes on price comparison websites. All quotes received were for 1 year contracts.
Mortgage	5	Based on 2, 3 and 5 year fixed-rate policies.[167]
Savings account	5	The FCA has found that easy access accounts opened 5 years ago or more have an interest rate, on average 0.82% lower than accounts opened within the past two years; this gap was 0.87% for cash ISAs.[168]

[163] Anyone with contract for more than 1 year.
[164] Anyone with a contract for more than 5 years.
[165] Mortgages excluded from calculations due to likelihood of skewing results.
[166] European Commission, Digital single market: user's rights.
[167] Anyone on a policy which lasted longer than the duration of the fixed rate was classed as moving onto a standard variable tariff.
[168] FCA, Price discrimination in the cash savings market, July 2018.

All respondents who had been in a contract for longer than the maximum contract lengths we identified in any market were classed as paying a loyalty penalty.

Estimating the total annual cost of the loyalty penalty

Our researchers carried out extensive desk research to identify the individual costs associated with the loyalty penalty in each market. This used a combination of external publications and data provided by regulators and providers. Full figures are included in Data Appendix 3.

To quantify how many people were paying the loyalty penalty in the mortgage market, we used data collected by the Bank of England. To quantify how many people were paying the loyalty penalty in the broadband, home insurance, savings and mobile handset markets, and for how long, we used data from a survey run by ComRes in July 2018.[169] Data was weighted to be representative of the GB population. We also recorded data about the respondent's gender, age, household income, level of education, mental health, region, tenure and ethnic group.

We used this polling to weight costs gathered through desk research by the length of time a loyalty penalty was incurred. This was weighted again by the number of people incurring this penalty during each time period to reach a total cost for each group of time spent paying a loyalty penalty. Our researchers used ONS population data to extrapolate to how many GB households were paying a loyalty penalty.[170] In general, these are more conservative figures than the number of people we identify as affected by the loyalty penalty in total, due to our ability to determine concretely how much and how many we expected to be paying our loyalty penalty figures. £4.1bn is therefore likely to be an underestimate.

The details of how the penalty in each market was calculated is listed in full below.

Table A3: Cost of loyalty penalty extrapolated to GB population

Market	Number affected	Cost of the penalty
Mobile handset	3,965,000 adults	£473,300,000
Home insurance	12,350,000 households	£708,500,000

[169] Citizens Advice analysis of a ComRes survey of 3,030 British consumers in the energy, telecoms and financial services market.
[170] ONS, Estimates of the population for the UK, England and Wales, Scotland and Northern Ireland, Mid-2017, published 28 June 2018.

Broadband	11,300,000 households	£1,277,000,000
Savings	n/a[171]	£1,136,000,000
Mortgages	1,200,000 households	£526,800,000
Total		£4,122,000,000[172]

1. Handset inclusive mobile contract

The table below shows the average monthly loyalty penalty for consumers who have stayed in the same contract after the initial fixed deal ends.

Table A4: Cost of the loyalty penalty in the mobile handset market

Provider	High-range handsets (over £600)	Low (under £300) and mid-range (£300-£600) handsets	Across all handsets
Vodafone	£38	£19	£25
EE	£34	£16	£22
Three	£34	£17	£23

We calculate that 4 million consumers overpaid by £490 million over the lifetime of their previous contract. There are 50,644,000 adults (aged 18+) in Great Britain.[173] Our polling from July 2018[174] found that 43% of GB adults had a handset-inclusive contract as their last mobile deal, leaving 22,004,000. We focused on EE, Vodafone, Three and BT (combined market share of 51%)[175] as the only large networks that do not offer split contracts. This leaves 11,396,000 consumers whose previous contract was a bundled contract. Excluding 'don't knows' and people who switch either before, or as soon as their contract ended, 35% of bundled contract consumers (3,964,000) paid the loyalty penalty.

[171] The FCA Discussion Paper on price discrimination in the cash savings market did not provide details on the distribution of the loyalty penalty across different savings account. We have therefore not attempted to estimate the number of people affected in this market.
[172] Numbers do not add up due to rounding. For the purposes of this report, all figures have been rounded to 4 significant figures.
[173] ONS, Estimates of the population for the UK, England and Wales, Scotland and Northern Ireland, Mid-2017. Published 28 June 2018.
[174] An online survey of 3,030 adults in Great Britain conducted by ComRes for Citizens Advice, 18-25 July 2018.
[175] Ofcom, Nations and Regions Technology Tracker H1, April 2018.

We used Ofcom data on market share, and focus only on the 3 providers that did not offer split contracts at the time of publication.[176] Not all of the customers who are with the remaining networks (eg. O2, Virgin) will be on split contracts because you can't get a split contract through a third party retailer, and some customers will be on legacy contracts.

Table A5: % extrapolated to population

Months paying the loyalty penalty	% paying	Extrapolated to total customers
1-2 months after	13%	1,484,000
3-4 months after	6%	651,900
5-6 months after	3%	349,900
7-8 months after	1%	144,700
9-10 months after	1%	152,700
11-12 months after	1%	245,000
More than 12 months after	8%	936,800

We assumed that consumers stayed for the minimum number of months in each category (so those who reported 1 or 2 months we assumed to have stayed for 1 month outside the contract period, those who said 3 or 4 stayed for 3, etc.) For those who said they stayed more than 12 months, we assumed they paid the loyalty penalty for a full 12 months.

Desk analysis of 721 handset deals found the average handset loyalty penalty to be £22. So to find the average loyalty penalty for each group of people, we multiplied £22 by the average number of months that group are likely to have paid the penalty. We then multiplied this by the number of consumers likely to have paid that cost.

Table A6: Total handset loyalty penalty cost

Months paying the loyalty penalty	Average penalty per customer	Total number of customers	Total cost
1	£22[177]	1,484,000	£32,640,000

[176] Ofcom, Nations and Regions Technology Tracker H1, April 2018.

[177] Weighted by market share.

3	£66	651,900	£43,020,000
5	£110	349,900	£38,490,000
7	£154	144,700	£22,290,000
9	£198	152,700	£30,240,000
11	£242	245,000	£59,300,000
12	£264	936,800	£247,300,000
Total			£473,300,000

Difference between Citizens Advice and Ofcom estimates
Ofcom estimates that 1.5 million handset-inclusive consumers pay the handset penalty. This figure is based on survey data which shows that 6% of consumers on a handset-inclusive contract continued to pay their full monthly charge at the end of the minimum contract period, rather than taking a new contract with a new mobile phone or switching to a cheaper SIM-only service. According to Ofcom, this means that consumers could be overpaying by £330 million per year.[178]

This research measures how many people were paying the handset penalty at an exact point in time, and forms the basis of analysing the scale of overpayment on an annual basis. However, it does not include data on how long consumers pay the loyalty penalty for.

Our data enables us to estimate how long people overpaid for in months. Since the mobile loyalty penalty is paid per month, this gives us a more accurate picture of the total detriment incurred. Our estimates do not include consumers who have always had the same contract (i.e. those who have never switched). However, compared to the data gathered by Ofcom, our polling uses fewer questions to ascertain who is likely to pay a penalty. This places less of a burden on the respondent (in terms of time taken, recall and concentration), thereby increasing the accuracy of the data and minimizing dropout.

2. Home insurance

Data collected by the FCA in 2015 found that customers who renew their home insurance policy after 1 year pay on average 8% more than a new customer. And those who renew their policy over 5 years pay, on average, 70% more than new customers.[179]

According to the AA British Insurance Premium Index, the average cheapest premium in Q2 2018 was £163.03.[180] 8% of this is £13 and 70% is £114. Someone with the average

[178] Ofcom, Pricing trends for communications services in the UK, May 2018.
[179] FCA, Encouraging consumers to act at renewal, December 2015 (supplementary figures requested by Citizens Advice).
[180] The AA, AA British Insurance Premium Index – 2018 quarter 2, July 2018.

cheapest premium for combined home insurance pays an extra £13 after 1 year and £114 after 5 - regardless of claims or changes in circumstances.

Table A7: Home insurance loyalty penalty cost

Years since renewal	Average price difference to new customers (%)	Average policy price (£)	Average price difference to new customers (£)
0	0%	£163.03	£0.00
1	8%	£176.07	£13.04
2	27%	£207.05	£44.02
3	42%	£231.50	£68.47
5	69%	£275.52	£112.49
6	56%	£254.33	£91.30
7	55%	£252.70	£89.67

We have used this data to calculate the size and distribution of the insurance loyalty penalty since it is the most accurate data that currently exists. When estimating the number of people paying the loyalty penalty, however, we opted to use data from our nationally representative survey carried out in 2018 - rather than the data collected by the FCA as part of this investigation.

There are two reasons for this. Firstly, the FCA's data was collected in 2015 so may not be an accurate representation of the proportion of customers renewing at each stage. Secondly, the FCA's data shows the number of people renewing at each stage as a proportion of the total customers at the firm analysed. Since we wanted to estimate the cost of the loyalty penalty for the GB population as a whole, we also need to take account of the number of people who do not have home insurance (approximately 24% of GB consumers).

Table A8: Number of households paying different levels of penalty each year

Years since renewal	% of customers	Extrapolated to households
0	29.73%	7,859,000
1	14.73%	3,895,000
2	7.84%	2,072,000
3	5.54%	1,464,000

4	4.45%	1,177,000
5+	14.17%	3,747,000

However, our data cannot show the proportion of people who renewed their policy after the 6th or 7th year. We only know how many people renewed their policy between 5 and 10 years ago. In order to account for the slight decrease in the loyalty penalty after 5 years, we calculated the average price increase across 5-7 years (60%), and used this as the estimate of the loyalty penalty paid by all those who have had their policy for 5 years or more.

Table A9: The average price difference between a renewed policy and new policy

Years since renewal	% price difference	Cost of policy	New vs original cost
0	0.00%	£163.03	n/a
1	8.00%	£176.07	£13.04
2	27.00%	£207.05	£44.02
3	42.00%	£231.50	£68.47
4	52.00%	£247.81	£84.78
5+	60.00%[181]	£260.85	£97.82

Assuming that the proportion of people renewing multiple times remains constant over time, this means that each year, households will be overpaying by a total of £708,500,000.

Table A10: Total cost of the penalty each year

Years since renewal	Number of customers	Extra cost per person	Total cost per group
0	7,859,000	n/a	n/a
1	3,895,000	£13.04	£50,800,000
2	2,072,000	£44.02	£91,190,000
3	1,464,000	£68.47	£100,200,000
4	1,177,000	£84.78	£99,760,000
5+	3,747,000	£97.82	£366,500,000
Total			£708,500,000

[181] Average of 69%, 56% and 55%.

3. Broadband

Of people responsible for paying household bills, 43% began their current broadband contract 3 years ago or more. The longest contract identified by Citizens Advice researchers was 2 years - so these households are highly likely to be have paid the loyalty penalty for at least a year. This is the equivalent of 11,300,000 households.

The average yearly loyalty penalty in the basic broadband market is £113. We estimate that the broadband loyalty penalty costs households £1,277,000,000 each year. We chose to extend the loyalty penalty for dual play contracts across the whole of market for simplicity, since the weighted average loyalty penalty across dual play, triple play and quad play (using Ofcom's Pricing Trends Data) is very similar (£112).

In estimating the original broadband loyalty penalty, 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 TalkTalk. 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 was 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.

Table A11: 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 deal	Fixed contract cost	Cost after fixed contract	% increase	Monthly difference	Penalty per year[182]	Penalty over 4 years
BT 12 month	£24.49[183]	£40.99	67%	£16.50	£198.00	£594
Virgin Media 12 month	£32.25	£32.25	0%	£0.00	£0.00	£0.00
TalkTalk 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

4. Savings accounts

There are two main kinds of easy access savings account - a cash savings account, and an easy access cash ISA. According to the FCA's Cash Savings Market Study, both these account types earn less interest when the account was taken out more than 5 years ago. We have therefore calculated the loyalty penalty across both account types. All data used to calculate the market-wide savings loyalty penalty comes from the FCA's Discussion Paper on introducing a Basic Savings Rate, published in 2018.[184]

[182] Yearly difference between initial fixed contract period and after fixed contract period
[183] This is a time limited offer.
[184] FCA, Price discrimination in the cash savings markets, July 2018

Cash savings accounts

The total balance held in easy access cash savings accounts is £354bn. 33% of easy access balances are held in accounts opened over 5 years ago. £116.8bn is held in these accounts.

Easy access cash savings accounts opened more than 5 years ago have interest rates on average 0.82% lower than accounts opened within the previous 2 years. So each year, balances in these accounts could be earning 0.82% more in interest than they currently do. This is equivalent to £957,900,000 (0.82% multiplied by £116.8bn).

Easy Access Cash ISA

The total balance held in easy access cash ISAs is £108bn. 19% of these balances are held in accounts opened over 5 years ago. £20.52bn is held in these accounts.

Easy access cash ISAs opened more than 5 years ago have interest rates on average 0.87% lower than accounts opened within the previous 2 years. So each year, balances in these accounts could be earning 0.87% more in interest than they currently do. This is equivalent to £178,500,000 (0.87% multiplied by £20.52bn).

Adding these two figures together, the total annual cost of the loyalty penalty in the easy access savings market is £1,136,000,000.

5. Mortgage

In our 2017 report '*Exploring the loyalty penalty in the mortgage market*',[185] we estimated that 1,200,000 mortgage customers were overpaying by at least £439 each year.[186] That means a total loss of £526,800,000 each year. We calculated this loss using the following data:

We used data from the 2016 NMG/BOE survey[187] to extract demographic and mortgage information for those who are on the SVR and those paying fixed rates. This data is used to calculate the loyalty penalty - the yearly amount that mortgage payments would change if those on the SVR moved on to a fixed-rate mortgage.

To calculate the yearly loyalty penalty we have used results from the NMG/BOE survey alongside interest rates quoted on providers' websites on the 8th May 2017. A Citizens

[185] Citizens Advice, Exploring the loyalty penalty in the mortgage market, July 2017.
[186] According to the FCA's market study, only 5% of people on a reversion rate stay on this rate for less than a year. We therefore feel it is reasonable to assume that all those who pay the loyalty penalty pay it for a full year.
[187] The NMG/BOE survey (2011- 2017) asks respondents a series of questions about their financial position, including current mortgage debt on their main residence, whether the respondent has a repayment or interest-only mortgage, the type of interest paid on that mortgage, and the size of their monthly mortgage payments.

Advice researcher attempted to find the lowest interest rates available for 2 year and 5 year fixed products on the websites of 6 mortgage providers. These providers were chosen because collectively they represent 69% of gross mortgage lending in 2015, according to the Council of Mortgage Lenders.[188] The interest rates are listed in the table below. These were obtained by a Citizens Advice researcher inputting 'typical' first-time 20 buyer and SVR payer figures into providers' online mortgage calculators.[189] As noted above, all rates are for mortgages with product fees rolled in.

Table A11: Mortgage interest rates by provider and length

		First time buyer		**Typical SVR payer**	
Provider	**SVR**	**2-year**	**5-year**	**2-year**	**5-year**
Lloyds	3.74%	2.89%	3.09%	2.39%	2.94%
Santander	4.49%	2.14%	2.49%	1.64%	2.11%
Nationwide	3.74%	1.94%	2.64%	1.59%	2.04%
Barclays	3.74%	2.35%	2.45%	2.35%	2.45%
RBS	3.75%	2.79%	3.55%	2.59%	3.15%
HSBC	3.69%	1.69%	2.34%	1.54%	1.94%

When calculating the loyalty penalty, our analysis takes into account the fees and charges that mortgagors are likely or certain to pay when remortgaging, and could be obtained via the mortgage calculators on the websites of providers.

Valuation and account fees are subtracted from the loyalty penalty on an annualised basis.[190] We do this because all providers included in the analysis specify in their fees and charges documents that initial fees may also apply if switching to a new mortgage product. Mortgage providers also charge product fees, but usually allow customers to roll these fees into their mortgage in exchange for a slightly higher interest rate.

We have assumed that customers would roll product fees into the mortgage, and therefore we use these higher interest rates, alongside valuation and account fees, to calculate the annual loyalty penalty paid by SVR customers. Exit fees were not taken into

[188] Council of Mortgage Lenders, Largest mortgage lenders 2015 - challenger and specialist lenders show strongest growth in competitive market, July 2016.
[189] Interest rates for 'typical' SVR payers are those offered to customers switching their mortgage from a different provider.
[190] For example, where a combined £500 of valuation and account fees is charged for a 2-year fixed-rate mortgage, we have subtracted £250 from the annual loyalty penalty.

account, as they are rarely charged when remortgaging to a current provider.[191] Some providers may offer additional loyalty benefits, such as access to lower interest rate deals. We have not included such benefits in the analysis.

We calculated the loyalty penalty for typical SVR payers, which we defined by using the the average monthly payment amount (£651) and mortgage amount left (£60,000)[192] of SVR Interest rates for 'typical' SVR payers are those offered to customers switching their mortgage from a different provider. For example, where a combined £500 of valuation and account fees is charged for a 2-year fixed-rate mortgage, we have subtracted £250 from the annual loyalty penalty.[193] For first-time buyers, we used the UK's average house price of £219,000 and assumed a 25 year mortgage term and a 20% deposit.

Analysis by income

We performed an analysis of the 2017 ONS food and living costs survey.[194] This analysis was compared against our estimations of the cost of the loyalty penalty (£877), and used to determine proportions of expenditure by income decile.

Table A12: Loyalty penalty as % of household expenditure

	Expenditure per annum	**Loyalty penalty as % of per annum expenditure**
Lowest decile	£11,050	8%
Second decile	£13,707	6%
Third decile	£18,028	5%
Fourth decile	£22,210	4%
Fifth decile	£24,632	4%
Sixth decile	£28,626	3%
Seventh decile	£32,318	3%
Eighth decile	£36,572	2%
Ninth decile	£43,488	2%
Highest decile	£57,595	2%
All households	£28,818	3%

[191] Fee data were obtained by a Citizens Advice researcher on the 8th May 2017 via provider's websites.
[192] Rounded to the nearest £100.
[193] Payers on repayment mortgages in the BOE/NMG survey.
[194] ONS, Family Spending in the UK: financial year ending March 2016, released February 2017.

Appendix B: Our clients' experience of switching problems

Our researchers also analysed reports and evidence from local Citizens Advice offices and from the Consumer Service helpline to identify the type of problems people experience because of switching problems in these markets.

The nature of the cases that people come to Citizens Advice offices and the Consumer Service with tend to be related to immediate costs which are more common in mobile and broadband markets, rather than the long term creeping costs linked with the loyalty penalty in other markets. There is also a large disparity between the small number of cases encountered by local Citizens Advice, and the results of our polling. This indicates a lack of consumer awareness of the loyalty penalty in many of these markets.

Evidence forms submitted by local Citizens Advice

This super-complaint is illustrated using case studies derived from our Evidence Forms (EFs) and are based on the real experiences of Citizens Advice clients. The EFs used as case studies have been included as a separate document to this super-complaint, with all sensitive information removed.

Researchers searched EFs submitted by local offices over the last 3 years for people who had visited Citizens Advice offices for problems relating to switching essential services providers using the search term "switch". 237 EFs were coded by issue, sector and, if applicable, whether there was a cost attached.[195] Our analysis found the most common issues and median annual costs per person when switching in each market.

The table below shows how problems are distributed across these markets and median costs. A limited amount of cases for mortgages, savings accounts and home insurance affected these calculations. Local Citizens Advice offices likely see less of these issues due to the lack of an immediate financial impact in many cases.

[195] Attached as Data Appendix 4.

Table B1: Most common markets in Local Citizens Advice EFs

Market	% of cases	Median cost[196]
Mobile (including handset)	11%	£33
Broadband	80%	£275
Insurance	3%	£58
Mortgages	1%	0
Financial services	5%	£208
	Median	£240

Table B2: Most common problems in EFs

Market	Switching difficulties	Tariff changes	Switching advice	Tariff advice
Mobile (including handset)	75%	25%	0%	0%
Broadband	97%	0%	2%	2%
Insurance	100%	0%	0%	0%
Mortgages	100%	0%	0%	0%
Financial services	75%	0%	25%	0%

Cases from the consumer service

The Consumer Service is a helpline run by Citizens Advice for people to report consumer problems and receive advice on how to solve them. A Citizens Advice researcher carried out searches of Consumer Service records for any issues submitted over 12 months related to the loyalty penalty. The following key terms were used for this:

- Switch
- Switch*
- Loyal*
- Switching
- Tariff
- Switching supplier
- Changing supplier

[196] All costs are self-reported.

- Landline/Broadband/Mobile/Insurance/Savings Account/Bank* switch and/or tariff

If a search returned more than 400 results, we used the 400 most recent cases as a feasible number to analyse. A total of 1,352 unique results were included for analysis across the searches.

The consumer service covers all consumer issues, meaning these searches picked up many irrelevant results which also included the search term. These were removed from the full analysis, as were results for the energy sector. This left 236 cases for analysis. The results were further broken down by what type of problem was encountered and in what sector. Duplicate results were removed from the final analysis.

Table B3: Most common markets in the Consumer Service

Market	% of cases	Average cost[197]	Median cost[198]
Mobile (including handset)	34%	£200	£90
Broadband	61%	£196	£104
Insurance	3%	£105	£108
Mortgages	>1%	£65	£65
Financial services	2%	£1,075	£1,075
		£207	£100

Table B4: Most common problems in the Consumer Service

Market	Switching difficulties	Tariff changes	Switching advice	Tariff advice
Mobile (including handset)	62%	31%	6%	1%
Broadband	80%	16%	4%	>1%
Insurance	50%	17%	33%	0%
Mortgages	100%	0%	0%	0%

[197] Costs self reported or provided by case handlers.
[198] Costs self reported or provided by case handlers.

Financial services	40%	0%	60%	0%

Appendix C: Attitudes and awareness

Awareness of the loyalty penalty

Our ComRes polling of 3,030 people asked respondents whether they believed long-standing customers paid more, less, or the same as newer customers in each market. The percent of people who answered that long-standing customers paid more than newer customers were classed as being aware of the loyalty penalty and are shown in the table below. Our researchers crosschecked how aware of the loyalty penalty respondents were by socio-economic grade and age to identify the rolovere of vulnerability and income in the loyalty penalty.[199]

Table C1: Awareness of loyalty penalty

Market	Total respondents	Number aware of loyalty penalty	% aware of loyalty penalty
Mobile (including handset)	2,399	1,276	53%
Broadband	2,562	1,652	64%
Home Insurance	2,370	1,433	60%
Savings	2,047	840	41%
Mortgage	1,865	904	48%

We also analysed the impact that age had on the likelihood of paying a loyalty penalty and on attitudes towards switching. Young people were classed as respondents age 18-34, while older people were respondents aged 65+. The results of this are in the table below.

Table C2: Percentage of people paying loyalty penalty by age

Market	18-24	25-34	35-44	45-54	55-64	65+
Mobile (including	31%	42%	38%	33%	29%	28%

[199] Full statistical analysis in Excel files attached in Data Appendix 1.

handset)						
Broadband	22%	32%	42%	46%	45%	59%
Home Insurance	35%	53%	49%	41%	42%	54%
Savings	12%	19%	32%	46%	46%	54%
Mortgage	8%	12%	19%	11%	6%	2%
All markets	60%	80%	81%	83%	82%	87%

Our researchers also calculated the extent that non-participation in these markets affected these statistics.[200]

Our vulnerability analysis was supported by gathering data from our existing research and external publications. As part of this analysis our researcher also created a subcategory of mental health conditions that respondents with a mental health problem were diagnosed with 857 (61%) and 622 (45%) had depression and anxiety respectively.

Respondents were also asked how much they agreed with a series of statements about their provider and the switching process in each market. In each market, people who answered "I think I'm on the best deal" were crosschecked against those who were paying a loyalty penalty.

Table C3: Extent that all respondents agreed with the following statements

Market	I trust my provider	I think I'm on the best deal	Switching deals is too difficult	Switching deals is too time consuming
Mobile (including handset)	42%	35%	9%	8%
Broadband	39%	34%	11%	9%
Home Insurance	41%	36%	8%	8%
Savings	56%	22%	8%	8%

[200] Available in Data Appendix 1.

Mortgage	40%	32%	14%	10%
All markets	44%	31%	10%	9%

Table C4: % paying loyalty penalty who answered "I think I'm on the best deal"

Market	**%**
Mobile (including handset)	34%
Broadband	33%
Home Insurance	36%
Savings	20%
Mortgage	30%

Attitudes towards the loyalty penalty

Table C5: % of respondents who agree that long-standing customers should be charged the same as or less than newer customers

Market	**% agree long-standing customers should pay the same or less**
Mobile (including handset)	88%
Broadband	89%
Home Insurance	90%
Savings	88%
Mortgage	89%

Table C5: % of respondents who agree that providers should inform their existing customers when they are eligible for a better deal than the one they currently have

Market	**% of respondents**
Strongly agree	67%
Slightly agree	23%

Slightly disagree	5%
Strongly disagree	2%
Don't know	3%
Total agree	**90%**

Appendix D: Competition

For the purposes of this research, we identified the market shares of the dominant providers across essential markets, as outlined in the table below and in the competition chapter.[201]

Table D1: Concentration in essential markets

Market	Dominant providers	% market share
Broadband	5	91%[202]
Mobile (including handset)	4	86%[203]
Energy	6	77%[204]
Savings	6	68%[205]
Mortgages	6	75%[206]
Insurance	5	45%[207]

A Citizens Advice researcher used InFront analytics software to track the net profits of the leading providers in each of these 5 markets to identify market profitability. For companies not listed in InFront, publicly available data on net operating profits or profit after tax from annual reports was used.[208] Yearly profits were collected from a period of 5 years and averaged for each provider, then averaged across every sector. The raw results of these calculations are included as Data Appendix 2.

[201] The exception to this is the mobile contract (including handset) market. While 4 providers have the largest proportion of market share, for the purposes of this investigation we audited the 7 largest mobile service providers in the UK as included in Ofcom's complaints bulletin. This was to ensure comprehensive cover of the market in line with best practice.
[202] Ofcom, The Communications Market Report, 2016. This is the share of residential and SME broadband services. The providers are Virgin Media, EE, BT, TalkTalk and Sky.
[203] Ofcom, The Communications Market Report, 2016. This is share of retail mobile subscriptions. The providers are Vodafone, O2, EE and Three.
[204] Ofgem, Electricity supply market shares by company, 2017. The providers are British Gas, E.On, EDF, npower, Scottish Power and SSE.
[205] FCA, Cash savings market study: final findings, January 2015.
[206] FCA, Mortgage Market Study: Interim report, May 2018. The providers are Barclays, Lloyds, RBS, Nationwide, Santander and HSBC. FCA report states 'around three quarters' & the market shares are for balances of outstanding first-charge residential mortgages.
[207] IBISWorld, *Home insurance industry report*. The providers are AXA, Aviva, Direct Line, Lloyds and Royal and Sun Alliance. Refers to domestic property insurers only.
[208] Companies House, Vodafone Limited; Companies House, Direct Line Group; Companies House, Hutchison 3G UK Limited, Nationwide Building Society, Results and accounts.

Appendix E: Bibliography

Below is the full list of data published by external sources that we've analysed or drawn data from:

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Appendix F: Recommendations from previous reports

Appendix F collates our previous recommendations regarding the loyalty penalty, for ease of reference. As noted above, we do not regard these collectively as sufficient for tackling the loyalty penalty effectively; but represent the beginning of a conversation on remedies that could work.

Reviewing bundled handsets (2018)

- The 3 major providers still relying on bundled contracts - EE, Three and Vodafone - must stop charging for handsets at the end of the minimum contract period and should provide clearer pricing information.
- Ofcom should require providers to send more than 1 notification, and collect and publish data on the number of consumers beyond the minimum contract period by each provider.

Modernising consumer markets: response to Green Paper (2018)

- Make firms publish how much they are overcharging loyal consumers and take further, evidenced action to reduce price differentials in essential market.

The cost of loyalty (2018)

- Regulators should introduce targets for providers to reduce the loyalty penalty.
- Regulators and the Advertising Standards Authority (ASA) should improve framing of information across markets.
- Providers should be required to send much more effective, timely nudges.
- Providers and regulators should remove barriers to exiting a contract, making switching more straightforward and hassle-free. For instance, suppliers should commit to ensuring the same method used to enter a contract is available to customers who want to exit.
- Regulators should encourage the use of data and digital tools which help consumers to get a better deal.

The insurance loyalty penalty (2017)

- The FCA should require firms to ensure vulnerable consumers are on good value deals.
- Insurance providers should work with the FCA to improve market-wide systems for flagging vulnerability.
- The FCA should regard the loyalty penalty as a breach of their regulatory principle that firms must treat customers fairly.

Exploring the loyalty penalty in the mortgage market (2017)

- The FCA should require lenders to include clear, upfront and standardised information, in addition to the APR, about their SVRs before agreeing a mortgage with a new customer and when informing existing customers of interest rate rises.
- People should be able to choose when and how their provider contacts them to inform them their fixed rate deal is due to expire.
- The 'standard variable rate' label should be changed to better describe the nature of the contract.
- All mortgage deals should be available to all eligible consumers.
- The FCA should do further research into how the complexity of the fees involved in remortgaging puts people off switching.
- The FCA should monitor the detriment of the mortgage loyalty penalty to vulnerable consumers.

Exploring the loyalty penalty in the broadband market (2017)

- Price comparison websites should include price information for broadband packages beyond the minimum contract period.
- 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.
- Ofcom should monitor the development of the loyalty penalty and take further action if detriment continues.

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