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Dear Mark

CONSULTATION ON THE NEW PHONEPAYPLUS CODE OF PRACTICE

I welcome the opportunity to offer comments as part of your consultation exercise. I am a former Chief Executive of PhonepayPlus and am responding in a personal capacity. My comments are based in part on my understanding of the market and from experience in other regulatory fields, but also from research and policy work I have done for commercial clients and for an overseas agency also dealing with phone-paid services.

My response is limited to a number of, I think, critical issues. I do not propose to respond to the 62 questions in the main consultation document or all of the questions in the Summary Document.

My points relate to the outcomes-based approach, to the effectiveness of regulation across and down the PRS value-chain, to customer service and to the regulation of the payment mechanism that is phone-payment and not just the service categories that might use the mechanism. Across these issues I seek to offer thoughts on whether the approach is one that will drive better behaviour, higher levels of compliance and consumer trust. I am not convinced this is improved by the approach planned or, indeed, that the regulatory approach is anchored in the right place.

Outcome - or principles - based regulation

I think the need to distinguish between desired outcomes and principles-based regulation is something more than a semantic issue. The "outcomes" as listed appear closer to core principles: that services be legal, not offensive, fair- honestly promoted and clearly priced, properly delivered, respectful of consumer privacy and underpinned by adequate customer services. These might then lead to broader outcomes around high levels of compliance, high levels of consumer and broad public understanding and trust, and in service provider/broad industry readiness to invest and innovate and a growth in the services making use of phone-payment.

On this basis the principles and supporting rules and guidance would be designed and assessed against their effectiveness in achieving the outcomes set. I think this is important because I am not convinced the broad approach to the value-chain – drawing compliance activity down the value-chain to service developers and promoters - is consistent with outcomes as listed, and consumer protection and trust in particular.

I do, however, wholeheartedly support a move towards principles based regulation and a Code framework that allows PhonepayPlus to anticipate and/or respond quickly to market and product developments in ways found difficult in the past with a hard-wired prescriptive Code incapable of fast revision.

Regulation across the value chain

I welcome the proposition that all parties in the value-chain should be subject to appropriate regulation and that you should do more to establish meaningful standards in relation to risk assessment and due diligence. I am not convinced, however, of the strength of a regime if the reality is that the only substantive accountability for services rests with "Level 2 service providers": those who design or rent and "white label" services..

The proposition appears contrary to much of the practice elsewhere where those responsible for the retail, payment, delivery and public interface take full or very considerable responsibility for the services delivered. This is certainly the case with broadcasting – a closely related field of great significance given PhonepayPlus' position as an Ofcom agency. Here we see significant regulatory responsibilities imposed at the top of the value on the basis that there has to be clear and assured accountability and this needs to be so parties the regulator is confident have the contractual and commercial power to influence the behaviour of their "suppliers". The same applies with food and other retail services, in financial services and in the operation of credit schemes. These parties – the broadcasters, the supermarkets and the credit card companies have the substance, vested interest and power to set the standards required of those with whom they contract or sub-contract.

In premium rate/phone-pay market in which mobile networks and to a lesser extent fixed line networks contract to take 10-50% of the revenue generated by services the duties on these networks appear terribly limited. Over the last two years PhonepayPlus completed around 120 substantive investigations into mobile content services, with most related to forms of subscription or different abuses of the Mobile Termination (MT) payment mechanism. These cases resulted in about £6m in fines, with higher fines and most serious cases appearing in the most recent year. There is no record of actions in relation to the 5/6 mobile networks involved in each occasion and, consequentially limited pressure on them truly to deal robustly with their contractors and sub-contractors as long as the consumer damage is seen as negligible or shared across all providers and is outweighed by the core business interest in communications services.

The need to address the payment mechanism as well as the services

I believe there is a desperate need to address the payment mechanism, and that this need is magnified by the current widespread use – and abuse – of MT payment.

More than 60% of mobile customers are on pre-pay. Billing information is very limited for these customers and billing narratives are little better for those with network contracts. Networks are under little or no duty to be clear on the mark-ups with calls from mobile to fixed lines. Networks are not supervised by Ofcom or PhonepayPlus in their management of short codes and there is no regulatory framework for managing how dozens of services can "share" a short-code creating further customer confusion. Networks are under no obligation to offer opt-out / premium text barring and I understand few if any do offer this at the present time. And while networks are anxious to reduce customer churn and build loyalty they are under pressures to constrain the cost of customer service – as has been evident from their general practice of referring PRS related calls on to aggregators or others.

Finally, and of some significance when looking at the concept of appropriate regulation of the payment service as distinct from the content services being paid for, networks have a limited ability or willingness to become involved in consumer re-credit arrangements when their commercial partners fail to meet the rules of principles set in the Code. All of these factors are influenced by the size and value of the phone-payment sector to networks but this does not alter the fact that the situation in terms of networks as a provider of credit to their customers bears little comparison with the services provided to those using other forms of financial credit.

Developments elsewhere

I think it is interesting in this regard to look at developments elsewhere and at some of the seeming strengths of the industry or statutory regulation of other forms of payment. My comments are far from comprehensive but the issue of practice elsewhere is surely of relevance and worth assessment by PhonepayPlus.

In Australia I understand there have been steps taken to empower consumers/parents over premium payment barring or spend controls. I understand similar strategic controls may have been applied in Norway and elsewhere in the EU.

In China networks took decisive action to replace the extended value-chains (and the role of aggregators) with direct contracts between networks and content providers. This approach, historically established by NTT DoCoMo in Japan and followed now by Apple and the iPhone, reduced the number of content provider and services on offer for a time but seemingly dramatically improved customer service, trust and the long term potential for data value-add services.

In the US "class actions" in Illinois and State invention in Florida was focused on the leading networks and their aggregator "agents": not so the end-of-chain providers of individual services. There too networks have taken action to impose more direct control on providers of services and the services provided.

In Ireland, where I have had some personal involvement the decision to bring regulation into the statutory realm has been followed by a consultation looking at shared pan-industry responsibility for refunds and a possible bar or cap on the use of MT payment.

Recent experience at home

I believe any move to regulate the payment mechanism has to be anchored as much in the responsibilities of those issuing credit (networks) as it is in the conduct of individual traders who are allowed to use this credit facility.

Under the Code arrangements proposed the exposure of networks and aggregators/Level 1 providers is no longer absolute in the case of the latter or there at all in the case of the former. The effectiveness of the new regime appears conditional on these parties as "credit issuers" and "merchant acquirers" in credit-card terms exercising a level of control not previously seen on what may prove to be a large number of paper or brass plate Level 2 companies in the UK and around the world. It seems important to know how networks, in particular, see the matter. In another market a network with considerable global presence offered the following "*OCPs cannot be held accountable for the actions of other entities in the value chain whether they are content providers, service providers or terminating operators whose actions are outside of OCP control*".

The majority of cases now investigated already appear to be handled under the so-called IP Pass-through arrangement: with PhonepayPlus agreeing to deal direct with the IP/Level 2 provider. Notwithstanding the declining size of the market an assessment of the 2009/10 complaints shows that the number of cases related to mobile content and MT payment is not falling and that the "average seriousness" of the cases is rising if this can be measured in rough terms by the size of fines imposed: up nearly 300% per case on 2008/9 levels. If the levels of fines imposed are a broad measure of the levels of consumer loss/detriment related to the "services" in question then it would seem that harm increased during 2009/10 and that this was still an issue long after tough measures were introduced in the first months of 2009. This is addressed further below in relation to one particularly troublesome form of mobile payment.

MT payment

The risks with such a situation appear to be magnified by the use of MT payments. This mechanism allows anyone with a contract through an aggregator to make direct deductions from the stored credit or post-pay credit of every mobile phone user in the UK – without the phone user knowing or having any possibility of taking any action to approve or refuse the payment.

This might just be tolerable if networks offered comprehensive customer services, spend/abuse safeguards, re-credit capabilities and seriously robust due diligence before they or their agents contract with new players. It is hard to see how those involved can argue this is in place when there is a published list of over 100 adjudications in 2008/10 with every case anchored in the use or abuse of MT payment. I believe the fines related to these cases exceeded £6million. This appears to a damning indictment of a payment mechanism that allows the unscrupulous to use consumer like cash points irrespective of the comprehensive and seemingly proportionate and clear rules that PhonepayPlus has developed in relation to individual service categories.

The problem, I argue, is with the payment mechanism, the limited infrastructure around it and the ability of those issue credit or acquiring merchants to limit their liability for what happens to consumers. The actions listed may be the actions of a minority but they reflect the risks inherent in the MT model and in a fragmented value-chain. If the industry collectively is unable to develop schemes that start genuinely to match the safeguards that come with other pay mechanisms I believe there must be questions over the continued across the board use of MT payment.

In Summary

A greater focus on outcomes is welcomed. The difference between outcomes and principles in regulating may need attention. But there is a need, unaddressed in the consultation, also to address the payment mechanism itself. This must mean more focus on the networks and the protection and service they offer their customers – and the responsibility they do or do not take for the conduct of all those with whom they share revenue. This is obviously anchored in the potential for refund arrangements at a network level – to all those with losses; not just complainants. I believe there is an urgent need specific action around the use of MT payments – a demonstrably flawed product in the current context.

If this happens then a readiness to focus more of the regulation related to the services themselves on level 2 content providers makes sense....and we could have the foundations for a wider, stronger, larger and more diverse phone-payment market. If this does not happen I am concerned that simple registration and limited due diligence responsibilities could lead to outcomes you are not seeking: continued abuse, low level of trust and use and further delay in building a genuinely robust valued e/t-payment mechanism.

Regards

George Kidd

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