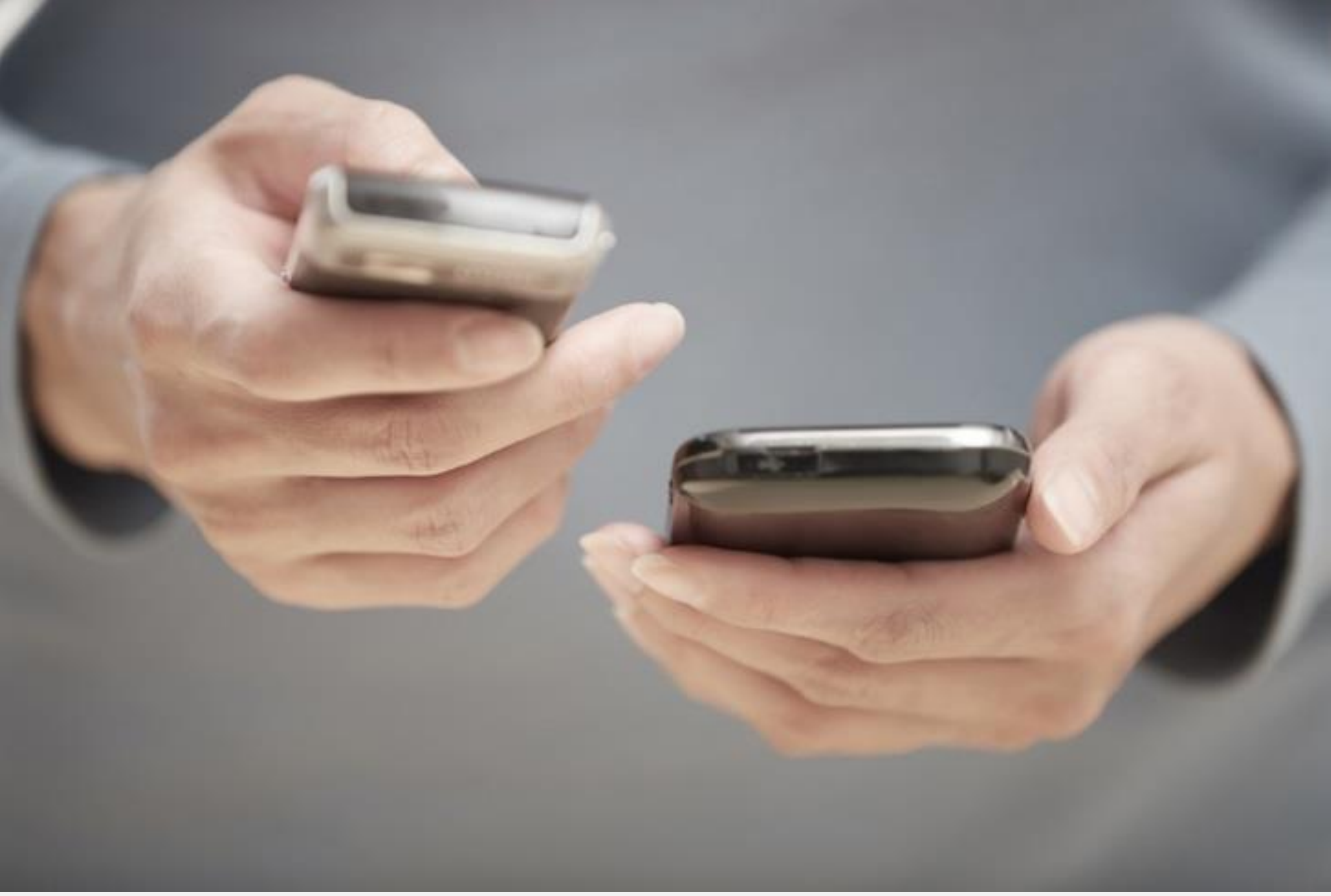


Vulnerability

A PhonepayPlus Discussion Document

PhonepayPlus

Contents:

About PhonepayPlus

PhonepayPlus is the independent regulator of premium rate services (PRS) in the UK, a role we have performed since 1986. PRS are added-value services which are charged above standard rate to a consumer's phone bill or pre-pay account. Popular examples include apps or in-app purchases charged to a phone bill, voting on TV shows, directory enquiry services and charitable text donations.

We are funded by industry yet retain robust regulatory powers delegated by Ofcom. Our goal is that anyone should be able to use any PRS with absolute confidence in a healthy and innovative market. In pursuit of this goal, we maintain a consumer-focused outcomes-based Code of Practice ('the Code') that establishes the standards for the operation, content and promotion of PRS and work collaboratively with industry to drive up compliance in the market. Where providers breach the Code we take robust regulatory action. In the last financial year we resolved 22,800 consumer complaints, levied £950,000 in fines and refunds to consumers in many cases and barred 17 providers from the market.

Summary

As the UK's regulator for premium rate services (PRS), PhonepayPlus has a responsibility to ensure that vulnerable consumers are protected from harm when purchasing digital content and services charged to a phone bill.

We have been assessing what the changing PRS and digital markets mean for consumers in general and vulnerable consumers in particular. The UK market for digital content is booming; it is estimated that it was worth £6.5 billion in 2014 and will be worth £14 billion by 2019[1]. But the risks posed to consumers and vulnerable consumers from the growth in digital content are poorly understood.

Consumers are now able to purchase goods and services in an instant without having to re-enter passwords or reach for the credit card. However, with payments increasingly easy to make, vulnerable consumers in particular could be exposed to running up very high bills unknowingly.

In a survey for PhonepayPlus 12% of parents said their child had run up a high bill when purchasing digital content on app stores like iTunes and Google Play - that would be equivalent to 900,000 children across the UK incurring instances of bill shock. This may be due to a combination of a number of factors that may relate to the consumer, how the service was promoted or the process by which it was purchased.

As a regulator, PhonepayPlus is committed to putting consumers at the heart of everything we do in a healthy and innovative market. Therefore we are assessing how PhonepayPlus should approach these emerging issues including how we should be working with other regulators and stakeholders. In protecting vulnerable consumers using PRS to access digital content, we commit to:

- Taking a proactive approach to regulation. We are acutely aware that market change requires a more flexible, coordinated approach to regulation. We aim to ensure that the risks faced by vulnerable consumers are mitigated by developing our Code, publishing new guidance and encouraging responsible innovation. Where malpractice occurs, we will continue to take enforcement action as provided for by our Code of Practice

- Ensuring we have the right powers. For instance, our Code enables us to implement spending caps on various services to mitigate the risk of bill shock.

- Having a comprehensive understanding of consumer vulnerability that acknowledges its dynamic nature.

[1] Deloitte Report on The Future for Phone-Paid Digital Goods and Services http://www.phonepayplus.org.uk/For-Business/~/media/Files/PhonepayPlus/Research/Nov2014_Deloitte_research.pdf

The changing market also requires an approach to risk management involving shared responsibility; protecting vulnerable consumers is not just about regulation but involves all market participants, including industry and consumers. Taking steps to protect vulnerable consumers benefits not only those consumers but the wider industry, by building consumer trust in the digital content marketplace. We recommend:

- Regulators operating in digital markets should collaborate to identify risks to vulnerable consumers, share best practice, enhance consumer awareness and ensure consistency of protection regardless of how services are paid for. We will also seek to engage the PRS industry, interested parties (such as academics and consumer groups) and new emerging providers in this dialogue.

- More help to consumers to help themselves to reduce the risk of harm, potentially through enhanced consumer protection tools and better communication of these tools.

What do we mean by vulnerable consumers?

We are moving towards a broader definition of vulnerable consumers that focuses on consumer vulnerability. Traditional definitions of vulnerable consumers divide consumers into the vulnerable and non-vulnerable. Consumers are vulnerable because of a particular individual characteristic. They may, for example, include those who are elderly or disabled.

However, this definition is narrow and static. It does not acknowledge that consumers can be temporarily vulnerable due to their situation or circumstance. For example, a consumer may be temporarily in a position of financial hardship or in a situation of bereavement. Nor does it acknowledge that a member of a vulnerable group in the tradition sense i.e. someone over the age of 65 is necessarily vulnerable all the time. A characteristics-based approach to vulnerable consumers also does not acknowledge that a consumer may be in a situation of transactional vulnerability that may arise from the nature of the good or service or the way in which they are purchased.

While a broader, more comprehensive understanding of vulnerability may be challenging for providers to implement, we believe it is necessary to ensure that all consumers are treated fairly and equitably.

Introduction

The issues faced by vulnerable consumers are at the top of PhonepayPlus' agenda for four reasons:

1. **Vulnerable consumers are more likely to use PRS than the average consumer.** Our consumer research states that 63% of vulnerable consumers had used a PRS compared to only 35% across all consumers during a six month period[2].

2. **Vulnerable groups such as children, older people and people facing financial hardship can be at risk of harm when using PRS.** Some PRS are designed specifically to serve consumers who are made vulnerable by their situation (e.g. services offering to find loans for people with poor credit histories). While the provider is offering services intended to benefit the consumer, particular care needs to be taken in the way that it is marketed.

3. **The market we regulate is undergoing a period of rapid change.** Changes in technology and consumer behaviour result in increasing convergence with other digital goods and services and payment mechanisms. In this period of change, it is essential that we keep abreast of the potential risks posed to consumers in vulnerable situations both in the market now but also in the future. It is also important that we look to digital goods and services paid for by other means to ensure risks are mitigated in a collaborative and co-ordinated fashion so that consumers are treated fairly and equitably.

4. **The price of some Premium Rate Services is going up.** Traditional PRS such as directory enquiries, online competitions and, as of July 2015, some live chat services are increasingly expensive. With the Money Advice Service estimating that almost half of adults do not have enough savings to cover an unexpected bill of £300 or more[3], the increasing price of PRS could have a real impact on vulnerable consumers.

One approach to protecting vulnerable consumers has been to investigate and adjudicate against providers found to have breached the Code rule concerning vulnerability (in addition to any other relevant rules of the Code[4]). We have found that this approach has had some success. Since the inception of our 12th Code in September 2011, our independent adjudications Tribunal has found

[2] Understanding Consumer Journeys http://www.phonepayplus.org.uk/For-Business/Research/~/media/Files/PhonepayPlus/Research/Consumer%20Research/PhonepayPlus%20Consumer%20Journey%20February%202014.pdf
[3] FCA's Occasional Paper No. 8: Consumer Vulnerability http://fca.org.uk/news/occasional-paper-no-8
[4] PhonepayPlus' 12th Code of Practice http://code.phonepayplus.org.uk/pdf/PhonepayPlusCOP2011.pdf

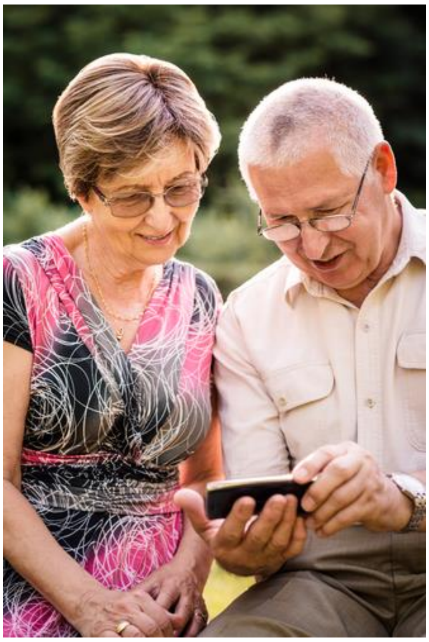
nine providers in breach of the vulnerable consumers' Code provision, imposing fines of £1.2 million. In the few cases where fines were not paid, providers were barred from the market for up to five years. In short, where providers have deliberately or recklessly taken advantage of vulnerable consumers, we have taken action, sending a message that such practice is simply unacceptable.

But we now believe that relying on traditional regulatory approaches to protecting consumers may no longer in isolation be the most effective means of fulfilling our regulatory obligations. In particular, we have been focusing our attention on understanding further:

- How the market is developing and what this means for consumers
- Whether the issues faced by vulnerable consumers are unique to them or similar to issues faced by all consumers
- How we can achieve a more comprehensive approach, involving prevention and collaboration as well as adjudication, in order to deliver more effective regulation
- How the regulators acting collectively can achieve better outcomes to protect vulnerable consumers

CASE STUDY: Targeting the Elderly

The independent Tribunal imposed a significant fine on a provider of word search competitions with prize draws on 087 and 09 numbers. The Tribunal determined that the provider's method of promotion targeted elderly consumers yet made pricing information difficult to comprehend. Pricing information was buried in the T&Cs at the bottom of the page, marketing was marked as urgent (in reality it was not) and prizes were far inferior to the quality claimed. All complaints PhonepayPlus received were either from elderly consumers or on their behalf, with some using the service on several occasions. The Tribunal imposed fines totalling £425,000 and required the provider to bring their service into compliance.



Regulatory Approaches to Vulnerability

Many UK regulators are reassessing their approach to protecting vulnerable consumers. The majority are moving beyond traditional understandings of vulnerability. Both Ofcom and Ofgem have published work on vulnerable consumers and vulnerability that view the issue of vulnerable consumers in a broad sense, focusing on the dynamic nature of vulnerability (as opposed to more static understandings of a vulnerable consumer). Ofgem, in particular, focus on the role of the market plays in combination with a consumer's characteristics to create situations of vulnerability.

The Financial Conduct Authority (FCA) is responsible for perhaps the most comprehensive body of work in this area published by a UK regulator to date. In their Occasional Paper Number 8, the FCA have looked to stimulate debate on vulnerability and offer guidance to the financial services industry on how to ensure they treat all customers fairly and equitably. Their definition of a vulnerable consumer is "someone who, due to their personal circumstances, is especially susceptible to detriment, particularly when a firm is not acting with appropriate levels of care."

A Changing Landscape

As a regulator, we need a clear picture of market developments to understand whether changes will pose new threats to vulnerable consumers in the future.

The UK PRS market is changing. Since 2010 the market has been declining by roughly 10% per annum. Services traditionally offered by providers are moving online and are often free. For example, free alternatives to voice services like directory enquires are available online often via a consumer's smartphone, reducing the use of directory enquiry (118) numbers by digitally savvy consumers. While the traditional industry is in decline, sectors like gaming, gambling and giving are experiencing growth[5]. Indeed, PRS is increasingly becoming a means of micropayment for digital goods and services billed to a consumer's phone bill or pre-pay account.

The market for digital content is growing rapidly. Deloitte predict that consumer spend on digital content will grow to £14 billion by 2019 from £6.5 billion today[6]. Smartphone and tablet penetration are key factors in driving market growth. With more than 70% of UK consumers now having access to a smartphone and more than half of UK households having a tablet, the majority are now able to purchase digital content using a mobile device[7]. Industry is responding to these trends. For example, games developers no longer make games for just PC and consoles but are increasingly focusing their attention on mobile opportunities.

The proliferation of devices are facilitating an 'always-on' culture, where consumers are able to access digital content whenever and wherever they want. This is in stark contrast to five or so years ago, when most digital content was still consumed on a PC or fixed line device. Consumers are now choosing to purchase anything from games, video, e-books and music through to cloud storage, educational products and physical goods on their devices. Put simply, consumers are able to purchase almost anything they want, at any time.

This trend is set to continue as younger consumers are at the forefront of market change. Increasingly, children own and use smartphones and tablets. 31% of 5 to 15 year olds have a smartphone, up from 20% in 2011. This figure jumps to 65% in the 12 to 15 age bracket. Tablet ownership is growing even faster. 34% of 5 to 15 year olds now own their own tablet, up from 19% just a year ago. While ownership is growing at a substantial rate, actual usage is significantly higher. 71% of children now use a tablet

---

[5] For greater discussion of the dynamics in the PRS market see PRS Annual Market Review http://www.phonepayplus.org.uk/~/media/Files/PhonepayPlus/News-Items/2015July/2014-Annual-Market-Review.pdf

[6] Deloitte Report on The Future for Phone-Paid Digital Goods and Services http://www.phonepayplus.org.uk/For-Business/~/media/Files/PhonepayPlus/Research/Nov2014_Deloitte_research.pdf

[7] Ofcom's Children and Parents: Media Use and Attitudes Report 2014 http://stakeholders.ofcom.org.uk/market-data-research/other/research-publications/childrens/children-parents-oct-14/

at home.

The Government now notes that 89% of young people use a tablet or smartphone to go online, up from 43% in 2010[8].

In the vast majority of cases, this changing consumer landscape is good for both consumers and business. Consumers have greater choice and businesses can connect to potential consumers the world over. Games or app developers can work anywhere in the world and almost instantaneously gain access to millions of consumers across international borders.

Purchasing content is also more seamless. The changing landscape has affected the services we regulate. For example, we regulate purchases made using operator billing (that is, when a consumer charges a digital purchase to their phone bill or pre pay account) as we do when a consumer purchases a traditional PRS. Operator billing is already popular as a relatively seamless and simple payment experience. This popularity is set to grow for those purchasing games and other digital content.

Our data suggests that the market for operator billing has more than doubled in the 2014-15 financial year as more and more consumers choose to charge digital purchases directly to their phone bill. Deloitte predict that the operator billing element of this market could grow to more than £500 million by 2019 .

We welcome such market developments. We launched a 12-month app store pilot in May 2014, where services purchased on app stores charged to a consumer's phone bill are regulated by PhonepayPlus. The pilot, with Google as a signatory, was designed to ensure that consumers have the same levels of protection and redress that they can expect when purchasing other PRS, but also tailors our regulatory rules to allow industry to develop new offerings, delivering greater consumer choice. Following a successful trial period, we confirmed the pilot in May 2015 meaning consumers can now purchase apps on the Google Play store (or other qualifying app stores) using their EE, Three or O_2 account. Consumers are already turning to operator billing in their thousands, enjoying a seamless payment experience with the safeguards that well designed regulation brings. If things do go wrong, consumers can now contact us and we can help them seek redress.

[8] Ofcom's Children and Parents: Media Use and Attitudes Report 2014 http://stakeholders.ofcom.org.uk/market-data-research/other/research-publications/childrens/children-parents-oct-14/

Emerging Threats[9]

New payment methods allow consumers to purchase goods and services in an instant without having to re-enter passwords or reach for the credit card. Examples include PayPal, Zapp and Apple Pay. For the vast majority, this is a positive development. But in some cases, such ease of payment carries risks, particularly for consumers in a position of vulnerability.

The numbers of consumers raising issues to us about digital content[10] and services have doubled in the space of a year to more than 160 per month. Complaints relating to digital content are now the third most common type of complaint we receive. We also know that vulnerable consumers are more likely than the average to use a micropayment. Our consumer research states that 85% of self-identified vulnerable consumers that have used a PRS[11] have paid for goods or services using a micropayment[12], compared to 55% of PRS users overall.

Bill shock. One of the most common complaints we receive is about bill shock. According to our consumer journey research, the average PRS complainant that reach PhonepayPlus have been charged £32. While this is not a new issue, the risk of bill shock increases as purchases become more seamless. Children are at particular risk.

A diffuse landscape. App developers can operate from anywhere in the world and gain access to a global consumer base through a digital platform like Microsoft's Windows Phone Store. While this facilitates greater consumer choice, seeking redress can be a challenge as developers can be difficult to contact. The diffuse nature of the landscape also makes it easier for scammers to hide from view. Identifying scammers, ensuring consumer redress and taking action against them is ever more difficult. It is therefore vital that the major content platforms play an active and responsible role in mitigating risk.

A growing digital divide. Both the opportunities and the problems discussed above relate to those consumers who – comfortably or otherwise – use digital services. But many, particularly older people, lack the confidence to take advantage of the internet, let alone of the rapidly changing digital landscape. The Office for National Statistics estimate that four million households do not have internet access, a third of whom

[9] We do not consider here threats that are less prominent in our remit or are being effectively tackled elsewhere. For example, the UK Council for Child Internet Safety (UKCIS) does an excellent co-ordination job in addressing young people's access to inappropriate content.
[10] We define digital content as all non-adult content downloaded to a mobile phone. This includes games and apps, ringtones and wallpapers. It does not include competition services and other quizzes, which are considered not to deliver content to a consumer's mobile phone.
[11] These are self-defined vulnerable consumers from a survey of 4,000 adult PRS users. http://www.phonepayplus.org.uk/For-Business/Research/~/media/Files/PhonepayPlus/Research/Consumer%20Research/PhonepayPlus%20Consumer%20Journey%20February%202014.pdf
[12] A micropayment is a small or very small financial transaction made to purchase a good or service electronically.

didn't have access because they felt they lacked the requisite skills. This is particularly prevalent among older consumers; 59% of households populated by one over-65 do not have internet access[13]. This growing digital divide means that people lacking digital skills or confidence may miss out on many opportunities and may be put to considerable inconvenience and expense. For example, the cost of calls to some 118 numbers has risen considerably in recent years and this affects older people who are not habitual users of the internet; their vulnerability to bill shock is in part due to their lack of digital confidence and skill.

Misleading promotions. Developers and PRS providers rely on digital channels to market their goods and services. In the vast majority of cases these are effective and compliant means of reaching consumers. However, digital marketing continues to be a source of concern both within and outside PRS; the digital environment allows promotions to be disseminated easily and cheaply to a broad audience meaning any misleading promotions can quickly cause problems. This is a particular risk for vulnerable consumers. First, children may lack the ability and experience to be savvy consumers of marketing material. Second, those lacking digital skills may, due to misleading promotions, either buy services they do not really want or fail to understand fully what they have committed to by making a purchase. This can be particularly problematic in relation to subscription services where charges are ongoing until stopped by the consumer.

Affiliate Marketing, Programmatic Advertising and Vulnerable Consumers

Vulnerable consumers have been disproportionately affected by PRS marketed using affiliates (third party marketing agencies employed to drive traffic to a service; in the case of PRS, they are often paid per customer conversion). In 2013-14, five of the six most severe cases involving vulnerable consumers brought before the PhonepayPlus Tribunal included affiliate marketing. We responded by issuing guidance to industry on using affiliate marketing, taking a robust approach to enforcement and working with industry to identify risks as they emerge to ensure that harm is minimised.

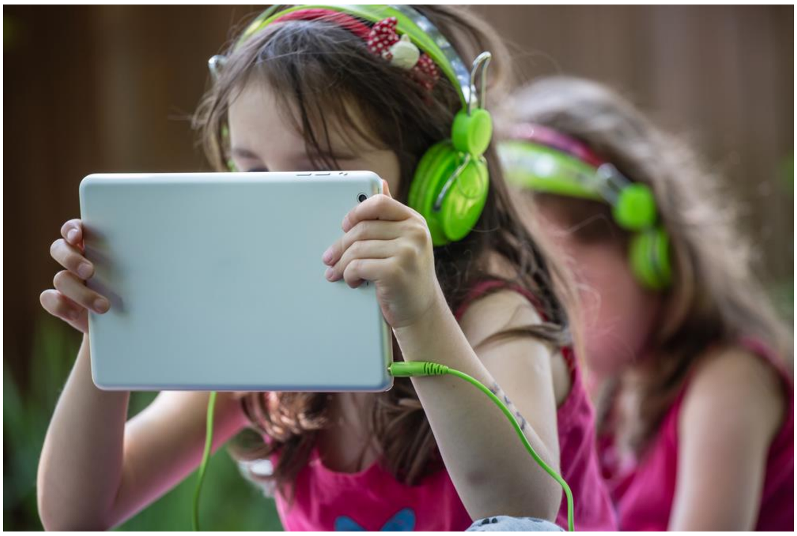
More recently, programmatic advertising has become an increasingly prevalent type of digital marketing used by PRS providers. According to the Internet Advertising Bureau, two thirds of all UK mobile advertising was purchased this way in 2014 . While programmatic advertising can be extremely effective, it does pose risks to consumers and businesses. We have seen inappropriate banner adverts place in apps clearly designed for younger consumers. These ads either leaded to adult material or, once clicked on, could result in premium rate purchases being incurred very easily and often without the consumer knowingly engaging in a service.

---

[13] Office for National Statistics http://www.ons.gov.uk/ons/rel/rdit2/internet-access---households-and-individuals/2014/stb-ia-2014.html

Regulatory change. Innovation is not the only source of market risk if not properly managed. There may also be increased risk during transitional periods while changes to regulation are implemented, even where the changes themselves are designed to increase consumer protection, transparency and choice. For instance, Ofcom have introduced a new tariff structure for non-geographic calls in July 2015[14]. The new pricing structure accompanies the introduction of higher rate PRS allowing providers of 09 services to charge up to £3.60 per minute plus an access charge, up from £1.53 per minute from a BT landline. Providers will also be able to levy a £6 initial connection charge for the first time. These changes are welcome – they will allow services currently operating on the 09 number range to compete with credit card and mobile short codes and make it easier for consumers to understand the cost of the call. But the increase in caps will represent a significant jump in the per-minute cost of some calls and could catch consumers unawares. Ofcom have launched UK Calling which is a dedicated website to communicate these changes. In turn, we are also raising awareness of these imminent changes.

Children and the changing PRS market



While we are moving to a more dynamic understanding of vulnerable consumers, children remain particularly at risk. The rapid growth in the use of mobile devices and tablets among younger consumers increases the prevalence of such risk. However, just as someone over the age of 65 is not necessarily vulnerable, not all young consumers are vulnerable in the same way. A fourteen year old may face different risks when using a mobile than, say, a seven year old. Add in other factors, like context, financial awareness and digital skills, and it is clear that younger consumers can be vulnerable in different ways.

---

[14] The unbundled tariff is an innovation Ofcom introduced in July 2015 to increase transparency around the cost of a call to non-geographic numbers (09, 087, 084, 118 etc.) from both mobile and landline. The total per minute cost of a call now comprises a ‘service charge’ paid to the service provider (e.g. 118118 or Ryanair) plus an ‘access charge’ paid to the consumer’s communications provider (BT, O_2, TalkTalk etc.). The new pricing structure fixes the cost a consumer pays per minute to their communications provider to originate any call be it from a landline or mobile to any non-geographic number. This ‘unbundled tariff’ structure is designed to make the total call cost clearer to consumers and avoid situations where consumers are unaware how much their mobile phone company is charging them on top of the per minute call cost to make a call.

Regulators and Government have generally focused on preventing children accessing inappropriate content and antisocial behaviour e.g. cyber bullying. These, clearly, are very important objectives. However, we are concerned that financial or commercial risks receive less attention. Our complaint evidence and research suggests that. We've identified three transactions or activities where younger consumers are more likely to get into trouble:

1. In-app purchases - Consumers are adopting the 'freemium' model as a preferred means to consume digital content, i.e. consumers download content for free and only pay for upgrades as and when they want. Only a proportion of consumers are currently willing to pay upfront for digital content. While this is generally a positive development, it does present risks.

We have seen a case where an 11 year old child ran up a £29,000 bill through in-app purchases charged to a phone bill: the child unwittingly spent more than the equivalent of the average annual wage in just a few weeks by continually purchasing upgrades in games like Call of Duty and Candy Crush.

Fortunately we were able to secure a full refund from the app store and have subsequently worked with the mobile network to put in place monthly spending caps to ensure this does not happen again. We can help when in-app purchases are charged to a phone bill. We have also seen many examples of children running up significant bills charged to their parents' credit or debit card, some of which are referred to us. In these cases we were unable to help because we do not regulate the payment mechanic.

2. Virtual currency – many games require consumers to use digital money when making purchases. For example, an in-app upgrade to a popular game may cost 1,000 gold coins, which is the equivalent to £5. Children have difficulty converting virtual currencies into actual costs. Our 2012 research suggested that nearly half of 11 to 16 year olds struggle to comprehend the real cost of virtual currencies.[15] We can assume that the proportion that difficulty will increase the younger the consumer is.

3. Banner ads – many developers choose to monetise their apps by selling advertising space. However, this presents risks. Providers who rely on third parties to place their advertising risk marketing their services inappropriately. For example, we've seen several examples of mobile competition or subscription services advertised in apps and games designed for children – one in particular mobile content service was marketed in a game 'bubbles for toddlers'. Children inadvertently click on the banner and can quickly enter into a PRS at significant cost.

[15] Children as Connected Consumers
http://www.phonepayplus.org.uk/~/media/Files/PhonepayPlus/Research/Children-as-connected-consumers.pdf

Parents are concerned; 12% of parents say their child has run up a high bill when buying apps or making in-app purchases regardless of payment mechanism.[16] That is roughly equivalent to 900,000 children in the UK. Of the complaints we have received relating to in-app purchases, half have involved children. Children tend to spend more too; in complaints involving children, consumer spend was twice the average across all complaints. It suggests that children and their parents are not always able to control their spending and mitigate the risks of high bills. While some digital content stores do allow parents to set password controls, such preventative measures are not completely effective at eliminating the risk of in-app PRS purchases. Only 10% of parents are aware that they can set limits to apps or in-app purchases on a phone or tablet.[17]

Indeed, as an increasing proportion of children own and use mobile devices, we and many parents are concerned about the risk that incidents involving high bills could escalate. More than 90% of parents welcome a spending cap as a means to reduce the risk of high bills[18] while 60% thought it was 'very important' to protect children from high bills.[19]

---

[16] Populus poll commissioned by PhonepayPlus. Research conducted between 15th – 17th August 2014.

[17] Ofcom Children and Parents' Media Use Attitude Report 2014 http://stakeholders.ofcom.org.uk/binaries/research/media-literacy/media-use-attitudes-14/Childrens_2014_Report.pdf

[18] The Impact of the Spending Caps Review on Premium Rate Services aimed at Children http://www.phonepayplus.org.uk/For-Business/Research/~/media/Files/PhonepayPlus/Consultation%20PDFs/2013_Code_Review/2014_Code_review_Research_PRS_Children.pdf

[19] Understanding Consumer Journeys http://www.phonepayplus.org.uk/For-Business/Research/~/media/Files/PhonepayPlus/Research/Consumer%20Research/PhonepayPlus%20Consumer%20Journey%20February%202014.pdf

Addressing New Threats

The changing landscape and emerging threats outlined above have clear implications for how we do our work and also suggest that our regulation can be fully effective only if is part of a more coordinated approach to risk management. Clearly, traditional regulatory approaches to protecting consumers from harm are no longer as effective as they once were.

What are we currently doing?

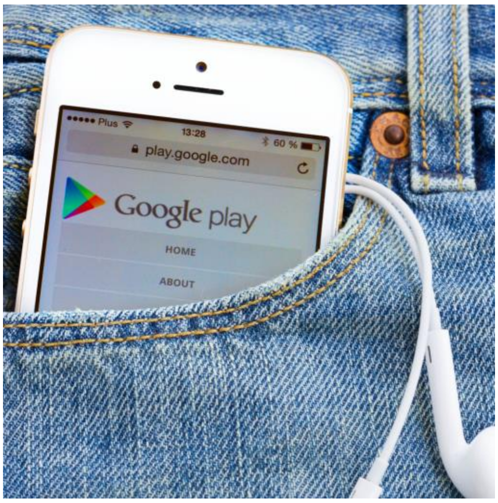
Putting vulnerable consumers at the heart of what we do by focusing the Code on outcome rather than intent. In our previous Code of Practice the provision dealing with vulnerable consumers applied only when it could be demonstrated that a provider had intentionally sought to take advantage of such consumers. This provided inadequate protection: vulnerable consumers are disproportionately the victims of services which harm them as the result of providers' recklessness as well as intent. Accordingly, as part of our review of the Code, we have changed the provision so that it focuses on the outcome rather than intent. This will not only increase protection for vulnerable consumers, but will also make the provision consistent with the Code more generally. As of July 2015, the new Code provision requires providers to exercise reasonable foresight as to who is likely to use their service and to take all reasonable steps to ensure that these customers are not at significant risk of detriment. If they have exercised reasonable foresight and a vulnerable consumer was to experience detriment, the provider would not necessarily be held responsible.

Modifying our approach to vulnerability and providing new guidance to industry. Traditionally vulnerability was understood in simple terms: a consumer was either vulnerable or not. While easy to understand, this categorisation takes no account of the fluid nature of vulnerability. In certain circumstances – such as when stressed or in an emergency – anyone may properly be considered vulnerable. For example, people experiencing isolation or those with a gambling problem may be vulnerable, but this is not captured in a simple binary definition of vulnerability, which may see a consumer as vulnerable because, for example, they are categorised as elderly on their 65th birthday. We intend to publish guidance, on which we will consult industry, regulators and consumer groups, which, we hope, will offer clarity and assistance to industry.

Pre-empting and preventing harm. In the past, our approach to protecting vulnerable consumers has focused on taking formal action against providers considered in breach of the Code. While this will remain a part of our regulatory approach, we believe a wider focus will protect consumers' interests and mitigate risk better. An approach that identifies risks early and encourages joint steps to mitigate them will benefit both consumers and industry. For example, we are actively contributing to an Early Warning System set up by industry to share information and potential risks in the market. Providers can then take action based on the information shared, controlling the risk of continued consumer harm before it gets out of hand. In short, consumer interests are best served by an approach which combines early joint preventative action with enforcement approaches when breaches have occurred.

Encouraging responsible innovation. While a rapidly changing market can pose risks to consumers, responsible innovation can deliver greater consumer choice and new and valuable services. We must use our regulatory powers in a way which allows responsible innovation to flourish while also ensuring proper outcomes for consumers. This requires us to keep on top of technological developments and to maintain a constructive and open dialogue with industry, in order to spot both opportunities and risks. Our twelve month app store pilot is an example, where a new business model required a fine-tuning of our regulation and a collaborative approach to risk management.

Piloting Innovation: Operator Billing and App Stores



As mentioned on page 8, we launched an app store pilot in May 2014 that aims to ensure consumers receive the same level of protection they receive with other PRS when purchasing apps or making in-app purchases charged to their phone bill. Throughout the pilot, we have worked with Google and Mobile Network Operators to implement measures that reduce the risk of bill shock. Google has introduced greater transparency of pricing and upgraded its payment authorisation process. EE and O_2 have also introduced measures to prevent excessive spend through spend reminders and caps. Since introducing these measures, we have seen complaints related to Google Play purchases decline. And in instances where consumers have incurred unexpectedly high bills, we have worked with both Google and the respective Mobile Network Operator to secure refunds as appropriate. Given the success of the pilot, we decided to make its conditions permanent in May 2015.

Other app stores are offering consumers the option of paying via their phone bill too. Microsoft, for example, allows purchases made on their Windows Phone app store to be charged to a mobile phone account. Consumers who select this payment option benefit from the safeguards our regulation offers. While consumers who choose a different payment means, e.g. credit card to pay for an app would benefit from certain protections, the level or this protection is not as high.

Other options: What more should we do?

The steps outlined above could achieve a great deal; but there is still more to do. We see two particular areas where we might be more effective.

Capturing complaints and sharing data. Our consumer journey research suggests that we may be underestimating the scale of the issues faced by both consumers in general but also vulnerable consumers using PRS. We know that vulnerable consumers are more likely to use PRS than the average consumer. Therefore we need to look at how we capture complaint data and consumer information. We also need to consider that we may never be able to collect perfect information and therefore sharing data with others will be essential. We are also working with the PRS industry to ensure that consumers can easily have complaints and issues resolved.

Capping purchases. Our previous Code capped one-off purchases on premium rate services aimed at children at £5 where alternative protections did not exist. This ensures that children are not unduly taken advantage of and that instances of bill shock are reduced. As noted earlier, more than 90% of parents welcome a spending cap, believing they reduce the risk of children running up excessive bills. We have bolstered the protections available to us by introducing a cumulative cap on PRS purchases of £20 per month. However, we are aware that the intended outcome of caps may be achieved by other means.[20] Changes to our Code retain our power to impose caps where necessary but also allows us to relax them if the best outcome can be achieved by other means.

What can others do?

Protecting consumers and ensuring an effective market are not matters for regulators alone. Regulators, industry and consumer groups share this responsibility and should coordinate an approach to risk management which works in the interests of consumers, particularly vulnerable consumers, as well as of industry.

Coordinated regulation. Many of the issues discussed in this paper cross the remit of several regulators; a number of regulators have responsibilities for aspects of digital markets. For example, the Competition and Markets Authority recently published principles for app developers. The Advertising Standards Authority is also responsible for regulating the advertising of products online. We are responsible for regulating PRS, including apps paid for by phone. Another example is financial services. The FCA has primary responsibility for regulating financial services in the UK and the Payment Services Regulator regulates the UK payment systems industry; but consumer credit brokerage services may use PRS billing, and so are regulated by us. Regulators should

[20] Our app store pilot identified that many major app stores have alternative means to protect minors from bill shock. As an outcomes-based regulator, we are open to providers meeting the objectives of the Code by other means. As a result, we launched a twelve month trial with app stores to explore whether they can meet the intended outcome of the spending caps without adhering to a strict cap.

share information and experience to ensure that consumer protection is consistent and reliable regardless of payment mechanic. Furthermore, regulators should not act in isolation.

Industry's role. Our Code already requires the PRS industry to design, operate and promote services in a way which does not take advantage of vulnerable consumers. But just as we are committing ourselves to an approach which pre-empts harm rather than dealing with it when it occurs, so should industry be more active in how it protects vulnerable consumers. Businesses should use all the tools available to them, such as complaint data and marketing expertise, to ensure that they are not taking advantage of vulnerable consumers.

Introducing measures to mitigate these risks also makes good business sense for the PRS industry: it will boost consumer confidence generally and reassure parents in particular, who, our research has shown, overwhelmingly believe that industry should take a lead in reducing the risk of children running up high bills. Indeed, as our Annual Market Review underlines, consumer trust is absolutely central to a healthy, innovative market. Many in industry have already designed and implemented such measures, but research suggests that they are being unduly reticent about publicising this: only 10% of parents are aware that some services allow them to limit app or in-app purchases on a phone or tablet. Of those parents who do limit such purchases, 95% value such features[21]. We strongly encourage industry both to strengthen and publicise such measures and to engage fully with regulators and consumer groups in achieving this.

Consumers' and consumer groups' role. Consumers and consumer groups also have a responsibility to understand the risks and communicate these as appropriate. For example, parents have a responsibility to educate their children on the risks of running up high bills. Consumers groups are ideally placed to understand the consumer experience and communicate the options available to consumers to mitigate risk.

[21] Ofcom's Children and Parents: Media Use and Attitudes Report 2014
http://stakeholders.ofcom.org.uk/market-data-research/other/research-publications/childrens/children-parents-oct-14/

Next steps

Through this paper we have identified two major underlying trends: both vulnerability and the market we regulate are by their nature dynamic. Traditional approaches to protecting vulnerable consumers in a changing market are less effective than they once were. As regulation in digital markets is converging, PhonepayPlus will continue to work with other regulators to identify risks to vulnerable consumers, share best practice, enhance consumer awareness and ensure consistency of protection regardless of how services are paid for.

We also commit to working with industry to provide new guidance for PRS providers to help them understand how they can treat all consumers fairly and equitably. Where necessary, we can also consider what guidance is available for consumers to ensure they understand what risks are posed by changes in the market and what they can do to mitigate these.

At this stage, we would welcome views from stakeholders as to the risks identified in this paper and the steps proposed to mitigate them. While we do not pose specific questions in this paper, the following may help respondents. Have we identified the right risks? If not, where should we focus our attention? Is a coordinated approach to mitigating risk realistic and proportionate? Responses would be welcomed within eight weeks of publication of this paper.

Where possible, comments should be submitted in writing and sent by email to Jonathan Levack at JLevack@phonepayplus.org.uk by September 30th 2015.