

# The ACMA's benefits estimation for the Telecommunications Consumer Protection code

## A PEER REVIEW PREPARED FOR THE ACMA

The ACMA has asked Frontier Economics to peer review its estimate of benefits from the implementation of the Telecommunications Consumer Protection (TCP) code. The TCP code was introduced in 2012, with elements being progressively introduced over the past few years.

For the purposes of the peer review, the ACMA supplied us with a (draft) written document outlining the methodology and results of the benefit estimations, and an Excel spreadsheet containing the benefit calculations. We have reviewed both the methodology and calculations in our peer review.

Overall, we conclude that the ACMA's estimates of the benefits of the TCP changes consumers are reasonable.

Some care would need to be taken before using these figures to support regulatory intervention, as some of the identified benefits may count as costs for industry.<sup>1</sup>

In the remainder of this note, we document our review and comment on particular inputs and assumptions.

## Overview of benefit estimations

The ACMA seeks to estimate the benefits of different kinds of behavioural change resulting from the TCP code:

- Benefits from **fewer complaints**, with benefits accruing to both consumers and to industry (including through reductions in required TIO funding to resolve disputes)
- Benefits from **better matching of customer usage patterns with available mobile plans**, so that there is less 'wastage' by consumers in the sense of spending more than they need to
- Benefits from **reductions in unexpectedly high bills**, where consumers' lack of information hinders their ability to acquire the desired level of service (and particularly usage of data services)

The ACMA's analysis suggests that the aggregate benefits to Australian consumers are in the order of \$545 million per year, with smaller benefits associated with reductions in consumer complaints and larger benefits associated with reductions in wastage from wrong contracts and from unexpectedly high bills.

## Estimation of benefits from fewer complaints

The ACMA's methodology is to estimate the reduction in complaints to the Telecommunications Industry Ombudsman (TIO) before and after the introduction of the TCP code. This reduction is converted into a dollar value which reflects the value of consumer and staff time saved. The benefits to consumers and to industry are estimated separately.

In our view, the method adopted is broadly an appropriate measure of benefits. Reductions in costs create more economic value – the difference between consumer willingness to pay and the costs of production.

On the specific estimation, we note that the estimates of complaint reduction should be built on a causal nexus between the introduction of the TCP code and reduced complaints. Ideally, this would involve:

- a good theoretical or principled argument that the TCP code would cause the identified effect (complaint reduction)
- an understanding of other factors that might explain the observed effect, and evidence or reasoning to explain why the TCP code effect is the more likely explanatory variable. This might be done, for example, by identifying whether the same kinds of results have been observed in similar markets but where the issues addressed in the TCP have not been resolved.

In our opinion, the ACMA does make out a credible case in principle that the TCP code may plausibly have caused a reduction in complaints.

The observation that there was, in fact, a reduction in complaints raises questions of attribution. Ideally, it would be good to see evidence that similar declines in complaints had not been experienced in other jurisdictions that were not subject to similar codes.

As the ACMA notes, some of the reduction in complaints may have been due to Vodafone correcting (perceived or actual) poor network performance through the years 2010-12. However, we also note that all three mobile operators experienced a reduction in complaints over the relevant period. This makes it more likely that the TCP code in fact was responsible for the falls in complaints.

Assuming that the attribution of reduced complaints to the TCP is reasonable, we consider the ACMA's estimation techniques and values chosen to be realistic.

## Estimation of benefits from reductions in 'wrong contracts'

Consumers can choose plans that are inappropriate for how they use their phones. In some cases, there will be objectively better plans that could be chosen (i.e. less expenditure for the same amount of usage and quality).<sup>ii</sup> Reductions in this

‘wastage’ were identified as a major potential benefit from the TCP, which introduced requirements for clearer information for customers to improve their ability to make choices.

The estimation of benefits by the ACMA relies on estimating the change in the aggregate waste from consumers in spending more than they need to meet their usage requirements.

The reasoning for *why* the TCP may have had an impact on consumers’ choices seems plausible.

Quantification of changes seems an inherently difficult thing to estimate. One would need to show that there is an objectively better plan that the consumer could have chosen that would have resulted in a cost saving without any reduction in the quality of service. For this reason, the ACMA relies on research initially conducted in the UK for its estimate of waste and transposes this to Australia. Given the difficulty of developing an estimate for Australia, the methodology applied appears reasonable.

The extent of reductions in wastage attributable to better information mandated by the TCP is also difficult to quantify.

The ACMA relies on survey information suggesting that around one-third of customers had seen a CIS and just under a third had thought the information made it easier to compare offers. This is not directly used in estimating benefits. Rather, the estimate of a 10 per cent saving in waste is based on customer contract turnover and the assuming that a proportion of those customers (1 in 4) are better informed and eliminate the waste as a result of the better information.

While the estimate is driven by an assumption, the analysis does indicate that the potential benefits from reductions in contract waste from consumers are large. Notably, the estimate only covers mobile services, with further gains that could be expected if the estimate was extended to fixed line and broadband purchases.

## Estimation of benefits from reductions in unexpectedly high bills

A reduction in unexpectedly high (mobile phone) bills is the major source of (consumer) gain identified in the ACMA’s analysis. It accounts for more than 80 per cent of the estimate benefits of the TCP.

The ACMA’s basic proposition is that the measures implemented to prevent unexpectedly high bills, such as mandatory alerts and better transparency of billing information, should have reduced the *instance* and *magnitude* of unexpectedly high bills.

The ACMA’s survey information indicates that:

- A third of consumers reported experiencing unexpected high bills within the previous 12 months in a 2013 survey.
- This reduced to 27 per cent in February 2015.
- The difference between the average unexpectedly high bill and average normal bill fell from \$158/bill in 2013 to \$125/bill in 2015.

The overall saving is the reduction in total unexpected bills – combining the effects of lower incidence, and each incident having a smaller impact.

In our opinion, these benefits are genuine but must be estimated and presented carefully. This is for three reasons:

- Declines in unexpectedly high bills might be explained by consumers ‘learning’ over time to avoid such high bills – even if there is no change in behaviour due to the TCP.
- Consumers derive benefits from additional usage, which reduces the *net* cost of unexpectedly high bills.<sup>iii</sup>
- A significant component of the savings experienced by consumers might well be transfers between mobile operators and consumers.<sup>iv</sup> Consumer benefits are experienced as losses by mobile operators.

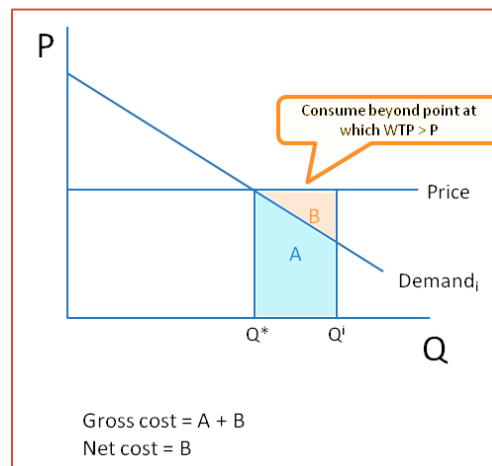
None of these factors is easy to account for, although we suspect they are all important. We also note that (to counter the last two factors) we would expect that to the extent that the TCP has increased consumer confidence in the price and quality packages offered by mobile operators, they may have encouraged higher demand than otherwise.

## Calculation issues

We have checked the calculations in the spreadsheets provided by the ACMA and confirm that they are accurate and consistent with the descriptions provided in the written materials.

## Endnotes

- i Such transfers are usually ignored in a formal cost benefit analysis.
- ii It is also plausible that some consumers choose plans that appear inappropriate for their usage profile but are valued because they provide the security of avoiding unexpectedly high bills or because they offer other benefits, such as a more valued handset.
- iii The 'loss' to consumers from unexpectedly high bills may be overstated, because it implies that consumers derive no benefit from the additional usage which the high bill has bought them. It seems likely that there is a net cost of the additional usage (the bill less consumer willingness-to-pay (WTP) for those units of usage), but that this would be lower than the gross cost which is represented by the bill (revenue). This may be illustrated using a simple diagram of a representative consumer. The representative consumer  $i$  has a downward-sloping demand for usage (of calls, data, etc.). This consumer might use 'too much' ( $Q^i$  rather than  $Q^*$ ) because of uncertainty about the price of additional usage of the service above plan limits. But that would not imply that the benefits of the additional usage are zero; the net cost to consumers would be 'B', not the total size of the bill 'A + B'.



- We also note this example as drawn may tend to underestimate the size of B relative to A. Although price is shown as constant per unit, pricing for additional usage often implies much higher per unit prices, which would increase the size of B relative to A.
- iv Benefits relating to better contracting and reductions in high bills are a benefit to consumers, but may be a cost for mobile network operators. That is, there are potentially significant transfers rather than increases in economic value (which is measured by changes in costs and changes in willingness to pay).