



connecting the future

Regulation of Buy-Now-Pay-Later Consultation

HM Treasury

October 2021

Response from The Payments Association

Introduction

The Payments Association welcomes the opportunity to contribute to HMT “*Regulation of Buy-Now-Pay-Later Consultation*”.

The community’s response contained in this paper reflects views expressed by our members and industry experts recommended by them who have been interviewed and who are referenced below. As The Payment Association’s membership includes a wide range of companies from across the payments value chain, and diverse viewpoints across all job roles, this response cannot and does not claim to fully represent the views of all members.

We are grateful to the contributors to this response, which has been drafted by Riccardo Tordera, our Senior Policy Manager. We would also like to express our thanks to HMT for their continuing openness in these discussions. We hope it advances our collective efforts to ensure that the UK’s payments industry continues to be progressive, world-leading and secure, and effective at serving the needs of everyone who pays and gets paid.

With special thanks to:

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Contents

The section numbering below corresponds to the numbering of the ‘questions for respondents’ in this paper.

1. Do you agree with our analysis of the business models that underpin the BNPL market?

Yes, we broadly agree with the analysis of BNPL product and services, and we believe it is important to create a distinction between BNPL and other forms of credit.

Whilst we welcome proportionate regulation, it is also important to ensure a level playing field by taking a holistic view and ensuring broader credit regulation is also fit for purpose and does not stifle innovation in the market.

2. Do you have information to provide government with a more granular and up-to-date understanding of the BNPL market?

We understand that BNPL usage continues to grow rapidly. According to a recent report (BBC news, 29.11.2021) around 17 million have used BNPL in the UK. Finder.com claims that almost 4 in 10 (37%) Britons say they have used a BNPL service. Over half (52%) of BNPL users have been using these services more often during the COVID-19 period¹. Data shows that BNPL is most popular amongst millennials, with 54% using this payment method. Further, we notice that BNPL is becoming a more widely accepted scheme, as its growth is not only from younger generations, but also from people aged 30-50.

Klarna was the most popular BNPL app, with 460,000 active monthly users in July 2020. 44% of shoppers use BNPL for its ease and convenience. Online purchases using BNPL services are growing at a rate of 39% per year, and almost ten million (9.5 million) Britons said they have avoided buying from retailers that don't offer BNPL options at the checkout.

3. Do you have further analysis or evidence of consumer detriment in the BNPL market?

At present, evidence published in the latest report from Citizens Advice² shows that consumer detriment is still very low. Only one in ten BNPL consumers are referred to debt collectors for missed payments, but this could soon rise to one in eight consumers.

Nonetheless, we remain concerned about the unresolved advertising and transparency issues, confusion when buying services rather than goods and the consequences of the current overlap with subscriptions and payments options where there is a liability for short term interest free credit.

¹ <https://www.finder.com/uk/buy-now-pay-later-statistics>

² <https://www.citizensadvice.org.uk/about-us/about-us1/media/press-releases/one-in-10-buy-now-pay-later-shoppers-have-been-chased-by-debt-collectors/>

4. Do you have analysis that would support us in identifying which specific elements of the BNPL business model pose particular risks?

While there is little or no published evidence, we believe the following elements pose particular risks to the BNPL business model:

- i. Impulse buying, tempting consumers to spend irresponsibly more than they planned or can afford, as per survey report from Which? (11.12.2020)
- ii. Lack of clarity about the credit agreement and general absence of warning about negative consequences if payment is missed or delayed. Citizens Advice research (03.09.2021) found that only 11% of those offering BNPL warned shoppers that they were taking out a credit agreement; the remaining 89% put this information in the small print or T&Cs.
- iii. Lack of assessment of creditworthiness or affordability for higher value purchases.
- iv. Significant risk of aggregate debt, where a consumer is able to take out multiple BNPL agreements with different providers. This may lead to excessive debt and a failure to make repayments. This is similar to holding multiple credit cards when credit cards first came into common use.
- v. Lack of consumer credit protection.
- vi. Lack of a standard process for consumers to file complain or report issues.

5. Do you agree with our analysis of the business models that underpin the short-term interest-free credit market?

Yes, we broadly agree with analysis of short-term interest-free credit products as distinct from BNPL services, although regulation should be business model agnostic to cater for the emergence of new business models. Concerns arise that consumer acceptance of using BNPL for small products is extended to more expensive short-term interest-free credit products with no regard for the increased risks.

6. Do you have information to provide government with a more granular and up-to-date understanding of the use of short-term interest-free credit?

We do not have any latest data to support a better understanding of this. However, we observe the following three different ways short-term interest-free credit is used:

- a) Discrete credit agreement for a specific higher value purchase or order
- b) Offered as customer credit account by Merchant directly
- c) New platform services which allow customer and merchant to connect directly with the lender at the time of transaction

7. Do you have further analysis or evidence that supports or undermines our understanding that there is limited consumer detriment in the short-term interest-free credit market?

We support the analysis that this does not share the same level of risk for consumer detriment that is seen in the BNPL market. Further, we believe that invoicing should be kept completely out of future regulation.

8. Do you have analysis that would support us in identifying which specific elements of the short-term interest-free credit business model serve to protect the consumer from harm?

We do not have any analysis to support this. We believe, however, that to protect consumers from harm, each credit agreement should be a discrete transaction and an assessment of consumer creditworthiness and affordability should be undertaken before credit is offered, supported by communication between various BNPL providers.

9. Do you agree with the distinction between BNPL and other forms of short-term interest-free credit that has been drawn in this consultation?

We broadly agree with this distinction.

10. Do you have any comments on our analysis of the drivers of risk for consumers in the BNPL market?

We agree with the analysis of the drivers of risk. The appeal of BNPL is that it's quick and simple to set up and easily available to any consumer. BNPL credit limits are generally small, and BNPL avoids the high interest fees of credit cards, but with frictionless purchases of many small value items, the overall sum, especially from multiple providers, can grow easily, and it is hard to keep track of the aggregate debt.

We believe that the variability between products of the consumer education provided about the terms of the agreement and the potential repercussions of non-repayment, should be recognised as a major driver of risk.

We believe, however, that BNPL will only be attractive to consumers if it remains quick and easy to set up, and available to the wider public. To this end, any regulation to make BNPL more secure will need to preserve these enhancing characteristics, while establishing clearer guidelines to clarify the information given to a consumer when they enter into a BNPL agreement.

11. Do you have any suggestions on how a clear distinction could be drawn between BNPL and short-term interest-free credit?

The first option (*restricting the extension of regulation to interest-free credit agreements where there is a third-party lender involved in the transaction, and keeping arrangements directly between a merchant and a consumer exempt from regulation*) would be more suited to allow for future variation but at the same time the A60F(2) exemption might benefit from being defined in further detail. Possibly, there should be a threshold over which BNPL would not apply.

12. Do you have any comments on the option to draw that distinction by restricting the extension of regulation to interest-free credit agreements where there is a third-party lender involved in the transaction? What impact do you think this would have on short-term interest-free credit providers that would be drawn into regulation?

We believe that there is a distinction to be made where third party lenders are incentivised to promote the use of BNPL over purchasing outright and this causes a potential conflict of interest. However, in most cases the third party involved in the transaction is already a regulated entity although it carries out unregulated activities. For these reasons we are broadly supportive of the extension. We believe that whether this is interest-free or not, every consumer loan should be regulated if undertaken via a third party. Hence, with this logic, there is no real impact on short-term interest-free credit providers because this is financed via sellers.

13. Do you have any comments on the option to draw that distinction by defining a BNPL agreement as one where there is a pre-existing, overarching relationship between the lender and consumer, under which the lender agrees to finance one or more transactions but where any repayments made are toward specific agreements made as part of that relationship?

We support this definition and agree that specific agreements for each transaction will help consumers to meet their repayment obligations and understand the risks of each transaction although, with each specific agreement and transaction, the consumer should be made aware of their cumulative liability.

Further, beyond the definition, rules should be based on the amount of credit involved in the transaction. There should also be a different set of rules such as the higher the value, the more restrictive the regulation of the credit.

14. Do you have any views on the need to amend the current exemption for running-account credit, so that it does not allow the unregulated BNPL model to re-emerge?

We would recommend allowing this to continue as is because this has enabled people to transact during the pandemic. One possible way forward could be to keep only the seller-based financing – exclusively made by sellers – exempt from regulation. In which case no other unregulated form of BNPL would re-emerge.

15. Do you agree that in any regulatory intervention merchants that offer BNPL as a payment option should not be subject to FCA regulation as credit brokers?

Yes, we agree with this.

16. If merchants offering BNPL are exempted from credit broking regulation, do you have any views on other ways to mitigate any potential risks to consumer detriment arising from merchants?

Mitigation could also be achieved with very clear, visible and transparent T&Cs to sign up to, and a clear explanation of what happens in case of failure to repay. Some of these conditions may need to be defined by the FCA, to avoid modification in favour of the lender / merchant and to ensure effective consumer protection. Mitigation could include a requirement on merchants to educate customers.

Beyond consumer detriment, there also should be some mechanism to protect the merchant not receiving the money owed. Some form of regulation and control will have to come into force as it is not acceptable to create a system without the provision of clear liabilities. Possibly, the only other way would be to impose some thresholds.

If merchants offering BNPL are exempted from credit broking regulation, we believe that whoever provides credit should still be subject to some form of regulation, specific to the requirement and at a relevant level.

17. Do you have any views on whether such an exemption from credit broking should extend to all merchants, or whether there should be limited exceptions (such as for domestic premises suppliers)?

Most of our members believe this should be extended to all merchants. Some believe there should be limited exceptions based on risk.

18. Do you think that the current requirements on BNPL merchants and lenders around advertising and promotion are sufficient?

No, we do not; those in existence do not seem to be very effective. BNPL arrangements should be covered within the financial promotion regime. More focus on avoiding high pressure sales tactics would also be welcomed.

19. If you think that the requirements need strengthening, would the application of the financial promotions regime be appropriate, or are there any features specific to BNPL products that warrant different requirements?

The application of the financial promotion regime would be appropriate even if specific features of BNPL products include a focus on digital sales. However, certain areas could benefit from some appropriate regulation, such as:

- a) requiring lenders' pre-contractual screens to provide customers with clear information on the negative consequences of taking out credit, such as arrears fees and debt collection;

- b) requiring lenders to adhere to the lighter-touch FCA requirements around adequate pre-contractual explanations, but not applying the full CCA pre-contractual information rules to BNPL products;

20. Do you agree that the approach to pre-contractual information outlined is consistent with a proportionate approach and the government's objectives for BNPL regulation?

Yes, we agree, and we believe that the full extent of CCA pre-contractual information is not appropriate for BNPL.

21. Do you agree with the government's assessment that BNPL agreements are likely to need bespoke form and content requirements?

Yes, we agree.

22. Do you have any views on what form agreements for BNPL should be required take, and what content they should contain?

A brief and clear form is desirable, explaining consumer risks and legal implications to help consumers understand the implications of the agreement they are entering into and the consequences of not repaying on time. At a minimum, it should apply the FCA rules on arrears, default and forbearance with requirements on how BNPL providers should treat customers in financial difficulty or communicate with borrowers who have missed payments, along with the CCA information requirements for customers in financial difficulty which give warnings to borrowers that a firm might take action against them and provide an opportunity for them to respond.

This is potentially more relevant as firms begin to prepare for the adoption of the FCA's Consumer Duty.

23. What are your views on applying CCA provisions on improper execution to BNPL agreements? Do you think the consequential sanctions for improper execution should apply to BNPL agreements under any regulatory intervention?

Yes, we believe they should apply. And we also think that regulation doesn't work if there are no consequences for failing to apply it.

24. What are your views on the role of creditworthiness assessments as part of a proportionate approach to BNPL regulation?

Creditworthiness and affordability assessments should depend on the amount of credit and the duration of credit as this might be excessive for very small transactions e.g. less than £50. But without data sharing it is difficult to assess the full extent of creditworthiness. A consumer can borrow different amounts from multiple BNPL providers as there is currently

no data sharing between the players in the market and data is also not shared with credit reference agencies.

Whilst it is important to have mechanisms in place to offer a market-wide view of a consumer's creditworthiness, it is vital not to remove options for those users such as young people without credit cards who may be prevented from using BNPL if stricter rules come into force. Any solution will have to consider such potential issues and enable the industry to continue innovating in a non-prescriptive way on how to assess creditworthiness beyond traditional ways, such as data-gathering from social media for example.

25. Do you have any views on whether there should be specific requirements for creditworthiness assessments for BNPL agreements?

Data-sharing between market players is vital for properly assessing creditworthiness specific to BNPL. Some form of regular communication between BNPL providers could ensure that consumers credit profiles are shared between lenders. This is something that should be facilitated rather than mandated by prescriptive regulation. Any solution should be future proof and allow for innovation to deliver the outcomes that customers want, such as through Open Banking / Open Finance.

26. Do you have any views on how BNPL agreements should be reported to consumers' credit files?

At present, all kinds of consumer contracts are reported on credit files. We agree that BNPL agreements should be reported, in the same way as for consumer lending. But the initial credit worthiness assessment could just be a soft mark against consumers credit files. Credit reference agencies' data updates are very slow, and it may take weeks to appear on credit files. This can cause issues in the BNPL customer journey where transactions happen very rapidly.

27. Do you have any views about how customers in financial difficulty should be treated under BNPL agreements?

We believe that a flexible approach on the basis of how the request to pay has been designed should apply, and proportionate regulation is needed. Customers in financial difficulty should be given the opportunity to develop a repayment plan but this should be proportionate to the amount of the transaction and there should be a threshold beyond which further credit should be stopped. Once again, data-sharing becomes crucial to prevent failure to repay.

More generally, education remains vital – if customers know they are in financial difficulties and are aware of the BNPL arrangements they are using, then they should be responsible for failing to pay back.

28. What are your views on the proportionality of applying CCA provisions on arrears and defaults to BNPL agreements?

According to the Citizens Advice research mentioned earlier, only one in ten BNPL consumers are referred to debt collectors for missed payments, but this could soon rise one in eight consumers. Of those who were referred to a debt collector for missed payments,

96% experienced a negative consequence.

Hence, standard and regulated rules are required to make sure consumers across all BNPL providers receives optimal level of assistance in financial difficulty.

29. Do you agree that under any regulatory intervention for BNPL, section 75 of the CCA should apply to agreements?

In principle we agree, despite believing that this is and may remain excessive for BNPL and that further consideration needs to be given to what is appropriate, based on this wider review of BNPL.

30. What are your views on amending the scope of the exemptions from elements of the CCA for small agreements to include BNPL agreements under £50?

Our membership did not gain consensus in relation to this question even though it seems preferable not to amend the threshold.

31. Are you aware of any currently-regulated consumer credit products, in particular those which are debtor-creditor-supplier agreements, that are routinely offered with values less than £50?

No, we are not.

32. Do you agree that under a regulatory intervention for BNPL, consumers should be able to bring a complaint to the FOS?

Yes, we agree but the consensus view was fear that the FOS could become overwhelmed. This could be avoided by:

- a) the use of thresholds based on aggregate liability below which a quicker resolution is allowed, such as the introduction of an insurance policy (similar to what happens for instance with card purchases); or
- b) an authority other than the FOS taking responsibility for managing complaints. This would ideally be an existing authority rather than a new regulatory body.

33. What impacts do you expect the regulation of BNPL would have on BNPL providers, consumers that use the product, and merchants that offer it as a payment option?

BNPL enhances financial inclusion because it makes it easier to provide credit to consumers who are not eligible for other types of credit.

Regulation should lead to fewer losses and a more efficient market, although it may limit competition in favour of the larger providers. Some consumers will be less likely to use BNPL products, so merchants may see sales via BNPL reduced, but these should include consumers who would have been unable to meet the agreed repayments.

The spirit and nature of the regulation will influence the impacts of the market, providers, consumers and merchants. If regulation is proportionate, dynamic and flexible, it will make the whole sector safer, growing the market and making it more sustainable. It should not detrimentally affect innovation for BNPL providers or the consumer experience and will increase trust among consumers with better protection.

Complicated, cumbersome, prescriptive and inflexible regulation, however, could detrimentally affect the opportunity for providers to innovate and cut consumers off from a useful source of credit.

We would welcome light-touch regulation which is appropriate for the range of credit and the duration of the credit terms. Since the new FCA Consumer Duty is likely to have a significant impact on product design through to contracts and enforcement, this should be a consideration when developing regulation in order to minimize potential detriment to consumers.

34. What impacts would you expect to see on persons with the protected characteristics mentioned above as a result of regulation of BNPL?

Hopefully, consumers will have a clearer understanding of BNPL, and fewer people of every age-group will fall into debt through BNPL that they cannot handle. This is not exclusive to persons with protected characteristics.

35. Do you have any views on how the government can mitigate any disproportionate impacts on protected characteristics?

There is no evidence to suggest any disproportionate impacts on protected characteristics. Considering the protected characteristics of age and disability in particular, we would recommend that that BNPL is not available to those below the age of 18 and that the nature of the agreement and the risks are presented up front and in the most accessible language possible.

About The Payments Association

The Payments Association (previously the Emerging Payments Association or EPA) is for payments institutions, big & small. We help our members navigate a complex regulatory environment and facilitate profitable business partnerships.

Our purpose is to empower the most influential community in payments, where the connections, collaboration and learning shape an industry that works for all.

We operate as an independent representative for the industry and its interests, and drive collaboration within the payments sector in order to bring about meaningful change and innovation. We work closely with industry stakeholders such as the Bank of England, the FCA, HM Treasury, the Payment Systems Regulator, Pay.UK, UK Finance and Innovate Finance.

Through our comprehensive programme of activities for members and with guidance from an independent Advisory Board of leading payments CEOs, we facilitate the connections and build the bridges that join the ecosystem together and make it stronger.

These activities include a programme of monthly digital and face-to-face events including our annual conference PAY360 and awards dinner, CEO round tables and training activities.

We run 5 stakeholder working Project groups: Inclusion, Regulator, Financial Crime, International Trade and Open Banking. The volunteers within these groups represent the collective view of The Payments Association members at industry-critical moments and work together to drive innovation in these areas.

We also conduct exclusive industry research which is made available to our members through our Insights knowledge base. These include monthly whitepapers, insightful interviews and tips from the industry's most successful CEOs.

See www.thepaymentsassociation.org for more information. Contact malik.smith@thepaymentsassociation.org for assistance.