the payments association

connecting the future

Regulation of Buy-Now-Pay-Later
Consultation Response

HMT
June 2022

Response from The Payments Association

Introduction

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

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 Head of Policy & Government Relations. 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:

- Annemarie Mahabir, VP – Principal Payments Consultant, Endava
- Manish Garg, Founder & CEO, Banksly

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The section numbering below corresponds to the numbering of the 'Government Response – regulation of STIFC' in this paper.

2.36 To enable a final decision to be made about the inclusion of merchant-provided STIFC, provided online or at a distance, the government is undertaking further stakeholder engagement to further develop its understanding of this part of the market (set out in paragraphs 2.15, 2.19 and 2.27).

The government welcomes additional insight from stakeholders on:

• Scale - including the potential number of merchants providing STIFC themselves, both in-person or online or at a distance, and the types of sectors they operate in; and
• Operation - including the way in which merchants administer and manage the provision of STIFC.

Overall, our comment to sections 2.15, 2.19 and 2.27 mentioned above is as follows:

2.15: We agree with the statement that STIFC offered online and at a distance could be a key driver of potential detriment if there are no regulatory controls, and should be regulated alongside BNPL for the reasons indicated in the review.

2.19: In the current economic climate, some merchants may not want to take on the risk associated with offering credit but, for those who do offer STIFC to customers to drive sales, this could lead to similar problems as BNPL if there is no regulatory control.

2.27: This could be a good opportunity for merchants to modernise their business models and take advantage of new technology and innovation.

Commenting on scale and operation, we can observe that the scale at which unregulated BNPL loans are being issued has caused concern, because the exemption in the Consumer and Credit Act (CCA)[1] is not directly regulated and consumers who use BNPL are not as protected as they would be for other financial products, such as credit cards.

Third-party providers have recently started partnering with merchants to offer this type of financing. Merchants pay a fee to the third-party provider who provides the money up-front to the retailer and takes on the credit risk.

STIFC can therefore be further split into two categories – credit offered by a merchant supplying the goods or services, and credit offered by a third-party lender.

[1] BNPL and STIFC both operate within an exemption to the Consumer Credit Act (CCA) of 1974. This exemption originally existed specifically for allowing businesses to offer deferred payments for goods and services, so long as: a) the loan was short-term, and b) the loan charged no interest.

With STIFC, however, credit is typically provided by mature lenders such as Tier One banks, who must comply with the FCA's regulatory frameworks. Because of the rules governing the policies of these lenders, they are not free to offer credit in the same free-and-easy way as BNPL. Even where these lenders have offered unregulated products, they have typically done so in a quasi-regulated fashion, with credit checks and credit reporting as standard.

For this reason, the government's consultation implied that STIFC was the less harmful of the two models (section 2.16). The government suggested (in section 2.10) that STIFC is the more likely to exist in an already somewhat-regulated state, since it is more commonly provided by lenders and financial institutions who already operate within regulatory frameworks.

However, as the ecommerce sector continues its exponential growth, the two models are starting to become more alike. BNPL is starting to be used for higher-ticket purchases, while also going omnichannel – appearing not just online, but in-store too. STIFC, meanwhile, is increasingly moving online. Thus, the government noted that the lines between the two models are starting to blur (section 2.11).

As the lines between BNPL and STIFC blur, it is becoming increasingly hard to tell which business model a lender fits into. Therefore, if only BNPL were to be regulated, there is a risk that lenders intent on remaining unregulated would pivot their business models to become more like STIFC. This would open the door to STIFC being abused in the same way BNPL has – and, were this to happen, the government would have to go through the regulation process all over again.

For this reason, the government has recommended that any regulatory changes should apply to both models – indeed, that it would be easier to treat the two models as one for the purposes of regulation.

Since it looks like full regulation will not come into effect until mid-2023 (meaning the time taken between the initial Woolard Review and measures coming into effect will end up taking more than two years), it is clear that the government must avoid a situation where they need to repeat this lengthy process.

Hence, the most natural course of action is to impose regulation that not only shores up the safety of BNPL, but imposes the same rules upon STIFC too. It is fair to say that easy access to unregulated credit has the potential to cause consumer harm and should be regulated to prevent this from happening.

Those that will be impacted the most by forthcoming regulatory changes are the companies that have acted less responsibly to date. This mostly applies to the unregulated BNPL market (although many BNPL providers have acted responsibly to date).

For companies that have exploited the lack of regulation imposed by the 1974 CCA, new regulatory measures will force them to change their business practices – which will have a positive impact on their customers and the wider industry. Meanwhile, those lenders – both in BNPL and STIFC – who are already following regulatory best practice will experience little to no impact.

Anti-avoidance measures should also include legislative changes to ensure BNPL providers do not switch to a running-account model in order to circumvent regulation by using the article 60F(3) exemption instead.

Furthermore, especially given how long the FCA is currently taking to process authorisation applications, there will need for a suitably long transition window to allow firms brought into the regulatory perimeter time to apply for FCA authorisation.

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 6 stakeholder working Project groups: Inclusion, Regulator, Financial Crime, Crypto and Digital Currencies, Cross Border 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.