

Buy Now Pay Later

Regulations and Ethics





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Background

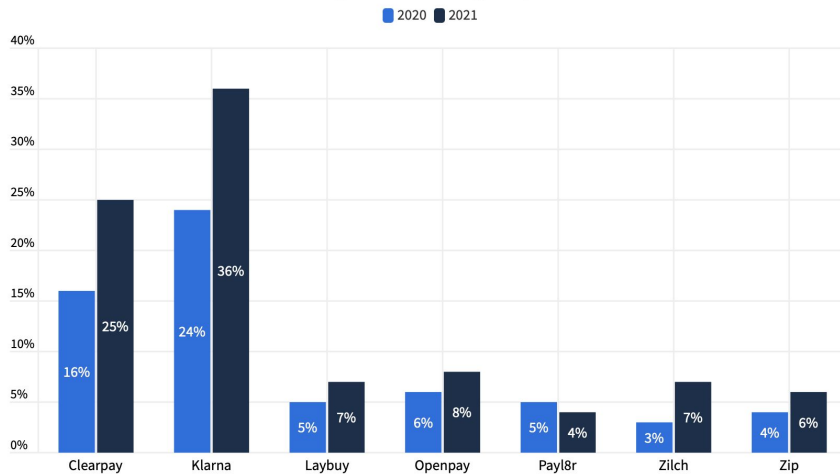
Buy now, pay later (BNPL) is a popular method for purchasing products online that helps **spreading the price of costly items across a few weeks or months** – making smaller monthly repayments rather than paying the full price in one go.

The BNPL provider pays the retailer for consumer. Consumer then repay the BNPL provider over a few weeks or months. The payment is normally interests free for the first 12 months.

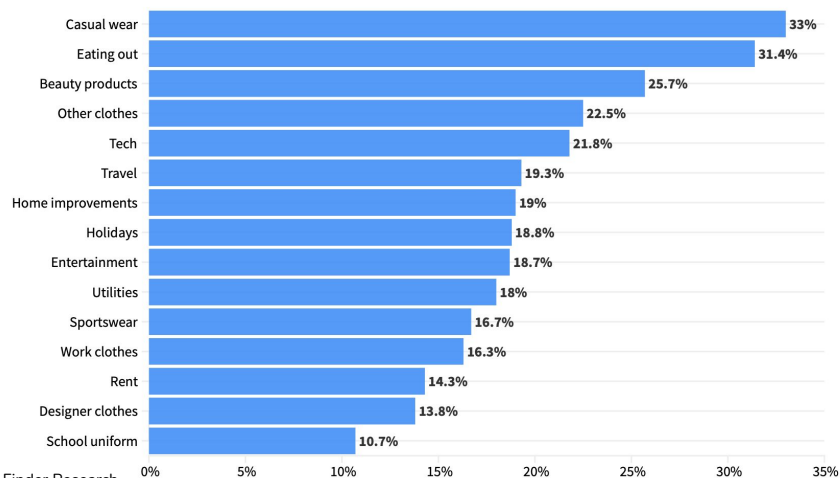
BNPL VS OTHER CREDIT SCHEMES

Buy Now, Pay Later is effectively a point-of-sale loan. BNPL providers make money by charging merchants a fixed or percentage fee for each sale, issuing the total cost of the purchase upfront and collecting repayments themselves. BNPL schemes require a “soft credit check” at checkout but typically do not alter a consumer’s credit rating.

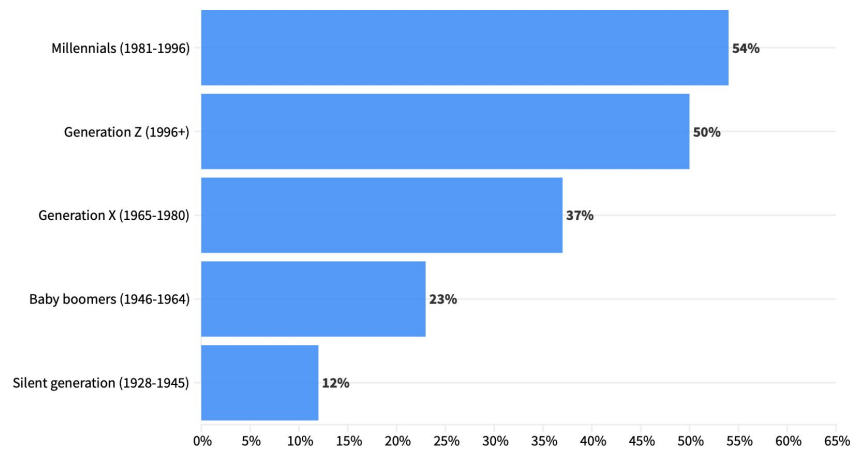
Percentage of consumers using BNPL platforms



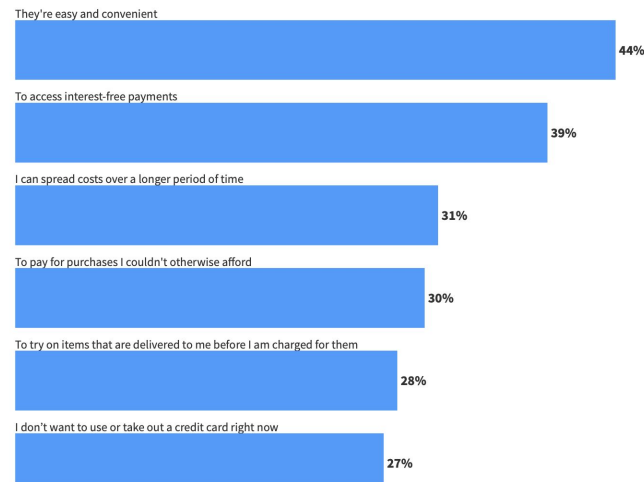
Product categories purchased by consumers using BNPL in 2021



Which age group is using BNPL services the most?



Why do shoppers use BNPL services?





Background - Pros & Cons

Pros

- Useful in times of inflation and high interest rates
- High credit scores are not necessary to qualify
- Approval process is fast
- May be more convenient than credit cards (due to no interest fees)

Cons

- Easy to miss payments (although, with Revolut, users are reminded of upcoming installments and notified if their balance is too low for the upcoming payments)
- Missing/late payments could result in additional fees and may impact credit scores
- Issues with restructuring payments when the item is returned
- No perks such as rewards or cashback (common in credit cards)
- Currently, consumers are not protected under Consumer Credit act.
- The knock-on effect for businesses can be considerable, resulting in cash flow disruption with potentially serious implications, particularly for smaller businesses and those in margin-tight sectors.



Controversials

Lessen borrower perceived debt risk

According to Citizens Advice, 40% of BNPL customers have had to borrow money to pay off BNPL debt and 1 in 10 customers didn't fully understand how the repayments would be set up

Forbes (2023) states that the average BNPL monthly debt among those 18 - 24 is slightly over 207 GBP

Out of all consumers that missed BNPL payments In June of 2022, 21% saw credit scores go down, 16% received calls from debt collectors, and 16% pays a late fee for missed BNPL payments

BNPL market share in e-commerce payment methods increased by five percentage points from 2019 to 2022



Current Regulations

- rules and guidance on advertising,
- the Consumer Rights Act 2015 concerning the fairness of contract terms, and
- the Consumer Protection from Unfair Trading Regulations 2008 in relation to unfair commercial practices
- Consumer Protection Legislation (taken step by FCA)

The Consultation, UK government plan to regulate BNPL

Scope of BNPL agreements under regulations

- ❖ are for fixed-sum credit to individuals or “relevant recipients of credit”¹
- ❖ are interest-free, repayable in 12 or fewer instalments within 12 months or less
- ❖ are provided by third-party lenders (i.e., a person who is not the provider of goods or services that the credit agreement finances)
- ❖ do not fall within one of the exemptions

Area of regulations

- ❖ creditworthiness assessments
- ❖ the provision of precontractual disclosures
- ❖ requirements on the form and content of credit agreements
- ❖ postcontractual information in the event of arrears, default, and forbearance.
- ❖ Financial Promotions
- ❖ Financial Ombudsman Service
- ❖ Distance Marketing regulations
- ❖ Section 75 - Consumer Protection

Behavioral Mechanisms

Personality Traits

High impulse-buying tendency, and low level financial literacy (which associated with higher assessment of benefits from, and lower assessment of risks) etc.

Present Bias

BNPL reduces immediate costs (shifting them into the future) whilst allowing consumers to purchase goods they want now, satisfying present-biased needs.



The effect of Friction

Frictions or decision points that add an extra moment to reflect on our choices. BNPL. Lack of friction in the current BNPL customer journey may help explain why some consumers may find themselves with a BNPL product without realising

Salience

BNPL checkouts tend to make some elements (including messages promising 'no fees') more prominent or eye-catching while hiding other information leading them away from important details (for example, information about late fees are often hidden).

Unregulated Behavioral Mechanisms

Nudging and Boosting

While the context around BNPL presents attractive nudges, little is done to prepare consumers to face the risks, benefits and procedures related to the service.

Incentives

Avoiding the interest rate loss is heavily appealing for consumers, especially when the BNPL message is framed in avoidance of the interest rate and not in other payment elements.



Online Friction Effects

The government's final policy position on BNPL states that the scope of regulation extends only to agreements offered by third parties. Stakeholder evidence deems regulating at a distance or online merchants as disproportionate.

Loopholes

There are exceptions which do not currently apply to BNPL. There is little protection, however, preventing BNPL providers from modifying their business model to a running account credit agreement model, for example.



Ethics

- ❖ Take advantage of financial illiteracy
- ❖ Promote irresponsible spending and enable many to rack up debts.
- ❖ BNPL services are often not advertised as a loan or credit, but a payment option, when they still have many of the same repercussions as loans when it comes to a lack of payment.
- ❖ BNPL can be compared to the greatly criticized payday advance and check-cashing loan industry. These short-term credits often result in the borrowers paying more on the interest rates than the amounts borrowed.
- ❖ Potential increases in materialism and the associated social and environmental risks
- ❖ Materialism risks associated with compulsive and impulsive consumption and credit overuse

Source:

<https://www.soprabanking.com/insights/buy-now-pay-later/>

Ku & Zaroff, 2014

Estévez et. al, 2021; Zhang et. al, 2016

Richins, 2011