



HM Treasury Regulation of Buy-Now, Pay-Later Consultation on Draft Legislation Submission by The Financial Inclusion Centre

About The Financial Inclusion Centre

The Financial Inclusion Centre (FIC) is an independent, not-for-profit policy and research group (www.inclusioncentre.org.uk). FIC's mission is to promote a financial system and financial markets that work for society. FIC works at two main levels:

Promoting system level change

Research and policy development to promote sustainable, resilient, economically and socially useful financial markets that: benefit the environment; encourage responsible corporate behaviours and create a positive social impact; and efficiently allocate long term financial resources to the real economy.

Ensuring households' core financial services needs are met

Promoting fair and inclusive, efficient and competitive, well-governed and accountable, properly regulated financial markets and services that meet households' core financial needs. We do this by: undertaking research into the causes of market failure in the sector; formulating policies to address that market failure; developing alternative solutions where the market cannot deliver; and campaigning for market reform. We focus on: households who are excluded from, face discrimination in, or are underserved by financial markets and services; and the intersection of finance, technology, and data.

Introduction

We are pleased to make a submission to this important consultation. At this stage, we are only able to provide a fairly high level response. We will respond in more detail when the FCA consults on the rules for BNPL.

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Summary of FIC submission

- We very much welcome the Government's decision to regulate BNPL and the determination to act quickly. As a non-profit organisation which focuses on financially vulnerable consumers and those poorly served by financial services, we have been concerned that these consumers have been left for too long without meaningful consumer protection when using BNPL.
- Access to fair, affordable, and sustainable credit that is *socially useful and enhances consumer welfare* is a critical aspect of financial inclusion and resilience. We emphasise social utility and enhancing consumer welfare as genuine financial inclusion is more than just about the numbers of consumers potentially having access to credit, or with credit. The fact that consumers can have easy access to certain forms of credit – or, more accurately, can be targeted with certain forms of credit as retail finance is supply side driven not demand led – is not necessarily welfare enhancing.
- There are three main types of consumer detriment in retail lending markets enabled by gaps in legislation and regulation or ineffective regulation:
 - Overselling and overconsumption of credit which can undermine consumers' propensity to save and build financial resilience. If it is too easy to borrow, it can make it hard to save. Overconsumption of credit can result in overindebtedness, leave consumers financially struggling, and exacerbate existing financial vulnerabilities.
 - The quality of loan products which can be high cost, poor value with unfair terms and conditions.
 - Negative impacts on consumer-focused competition. A permissive regulatory regime which prioritises enabling 'innovation', competition, and choice, and fails to constrain the growth in detrimental credit products, not only has direct negative effects on financially vulnerable consumers. It allows well-resourced commercial for-profit credit providers to crowd out non-profit community lenders such as credit unions and CDFIs who may be better placed to offer more appropriate credit.
- BNPL is often compared with payday lending. Indeed, BNPL seems to have taken the place of payday lending as a cause for concern. There are some differences. With payday lending, each of the three forms of detriment were evident.¹ The fact that there were few meaningful regulatory constraints on lenders meant it was too easy for consumers to borrow and for lenders to proactively target vulnerable consumers. Payday lenders were very efficient at using technology and behavioural finance insights to remove the friction between consumers and the act of borrowing. Payday lenders depended on consumer detriment for profitability. Once meaningful affordable lending standards and, critically, the introduction of a price cap were introduced the economics of payday lending no longer worked for most providers.

¹ [Payday Lending – fixing a broken market | The Financial Inclusion Centre](#)

- With BNPL, the terms and conditions may not be as egregious but the rapid growth of BNPL and the higher use of this form of credit by financially vulnerable consumers means the other forms of detriment are there in the market. In some ways, BNPL is riskier than payday lending as it is an even more efficient form of lending known as ‘embedded finance’. Embedded finance exploits the fact that the focus of the consumer is on obtaining the necessary or desired goods and services, not on the utility of the credit which facilitates access to those goods and services. BNPL providers have been very successful at removing any transactional friction that can cause consumers to consider carefully the decisions and choices they make.
- It is important to note that given the nature of embedded finance retailers who gain commercially from BNPL would ideally bear a share of the responsibility for detriment caused by BNPL. There is a two way relationship between the retailers and credit providers. BNPL providers could not sell credit without retailers creating the opportunities and retailers’ opportunity to sell goods and services would be restricted without BNPL. If the government does not want to bring retailers within the new regime, then greater responsibility will have to be placed on the BNPL providers to ensure that retailers promote access to the credit fairly and responsibly.
- We support the view that the appropriate information disclosure regime for the most part is best delivered through the FCA Handbook rather than the Consumer Credit Act (CCA). This should provide for a more flexible, agile approach to the provision of key information. But, it is important that this should not undermine the ability of consumers to exercise certain key rights in the CCA and should not remove the options of legal sanctions for failing to comply with requirements on information provision. The threat of legal action rather than regulatory action can be a powerful deterrent on corporate behaviours that harm consumers.
- More importantly, information disclosure as a regulatory tool has not proven effective at protecting vulnerable consumers. Vulnerable consumers are primed to borrow given their financial position and may have few good options to choose from. As mentioned, BNPL providers as with payday lenders before that, are very efficient at removing the necessary transactional friction that protects consumers. It is difficult to envisage the disclosure of information on its own providing meaningful consumer protection with embedded finance such as BNPL.
- We hope lessons will be learned from the payday lending market. It took robust product regulation and conduct of business regulation to support affordable and appropriate lending, constrain aggressive market behaviours, and inject friction into the marketing, distribution, and selling of payday loans. The payday lending market has significantly reduced in size, resulting in enhanced consumer welfare. A case of less is more. Obviously, price caps don’t have the same relevance for BNPL. But, robust regulatory interventions with regards to affordability will be needed to constrain the supply of BNPL credit to vulnerable consumers. Friction should be injected into the process to encourage consumers to stop and think about whether to borrow. In other words, the aim should be to deliberately impact the ‘customer journey’.
- We urge the Government to maintain its determination to quickly bring BNPL into the FCA’s remit so that consumers can avail of the necessary protections as soon as possible.
- The harm faced by vulnerable consumers using BNPL highlights the limitations in the current approach to regulation which relies on government legislating ‘innovations’ into the FCA’s perimeter. FIC argues for an approach based on purpose-based regulation where financial products and activities are presumed to fall within general categories based on their purpose. Categories of financial activities would then be presumed to automatically fall with the relevant part of the FCA’s regime with a very narrow set of exemptions. For example, if the financial activity in question is not the primary activity of a scheme provider – a case in point would be employers providing interest free agreements to employees. This approach would accommodate both dealing with financial activities which are likely to cause significant consumer detriment while still allowing lower risk activities to be covered by less robust rules and guidance. This approach would have caught BNPL much sooner.

- Linked to this, UK financial regulation has tended to be permissive, with policymakers and regulators intervening *ex post* after there is evidence of harm which cannot be ignored. The lessons of, for example, payday lending, rent to own schemes, motor finance schemes, advice on defined benefit pension scheme transfers² and, of course, BNPL itself provide salutary reminders of what can happen when government and regulators believe that activities *at the time* represent a low risk to consumers and therefore should not be fully regulated.
- It would be much more efficient and effective if regulators were given the powers to apply a more precautionary approach to financial regulation, particularly if combined with the purpose based definition approach outlined above. It is much better that harm is prevented rather than continually clean up markets after the event. *Ex ante* regulation is more effective than *ex post* regulation. Note that a precautionary and purpose based regime would not prevent the FCA from then using a proportionate approach to apply different regulatory expectations to specific types of firm (eg. for-profit versus non-profit).
- We would urge the Government to not limit the application of the new regime to agreements offered by third-party lenders. We argue the new regime should apply to BNPL generally not limited to third-party lenders. Increasingly, there is a blurring of the lines between finance and technology, and finance, technology, and retail consumer markets (known as ‘embedded finance’). Yet, the intersection between these markets is poorly regulated. Including only third-party lenders would create an obvious risk that big tech or e-commerce platforms would move into this market.
- We also disagree with the proposals to allow the sanctions set out in para 2.56 to fall away. We believe that while the majority of the day-to-day regulation of BNPL should be done under the forthcoming FCA regime, the existence of legal sanctions are also required to discipline the market.

List of consultation questions

Question 1: Do you have any comments on the proposed approach and/or drafting disapplying provisions on pre-contractual information (sections 55 and 55C)?

Question 2: Do you have any comments on the proposed approach and/or drafting disapplying provisions on the form and content of agreements (sections 60, 61 and 61A)?

The key here is to ensure that friction is, in some way, injected into the process of BNPL being sold to consumers. The goal should be to ‘impact the customer journey’ not to smooth the customer journey. This is particularly important as BNPL is a form of embedded finance. Consumers may not be focused on the social utility of the credit being sold to them at a time when the priority is obtaining the goods and services facilitated by that credit.

The Government could choose to: i. disapply sections 55 and 60 of the CCA altogether along with sections ; or ii. to retain sections 55 and 60 but disapply the various detailed requirements leaving it for the FCA rules to determine the details at a later stage.

We would prefer the second option. The threat of legal action in addition to regulatory oversight by the FCA would act as a further disciplining constraint on BNPL providers.

² Which were left outside of the Retail Distribution Review (RDR) reforms which banned commission payments to independent financial advisers

Question 3: Do you have any comments on the proposed approach and/or drafting disapplying provisions on ongoing information requirements (sections 77, 77A and 77B)?

Question 4: Do you have any comments on the proposed approach and/or drafting disapplying provisions on varying agreements (section 82)?

Question 5: Do you have any comments on the proposed approach and/or drafting disapplying provisions requiring prescribed information on early repayment (sections 97 and 97A)?

We support the proposed approach to ongoing information requirements. In the pre contractual stage, it is important to have points of friction to make it more difficult to sell the credit and encourage consumers to consider at a number of stages whether to take out the credit.

In the post contractual stage, the important point is to ensure that consumers can easily understand their position and BNPL providers take all necessary steps to communicate effectively with borrowers, identify vulnerability, and provide the necessary support under the Consumer Duty. Too much information can get in the way of these goals. These issues are best addressed by FCA rules.

Question 6: Do you have any comments on the proposed approach and/or drafting disapplying provisions relating to arrears, default and termination (sections 76, 86B, 86E, 87, 97 and 103)?

As above, we agree these issues are best dealt with through FCA rules.

Question 7: Do the amendments to section 129 and section 86 sufficiently retain the effect of these provisions for BNPL agreements?

We would argue that the right to apply for a Time Order should be retained to provide a backstop to Breathing Space, and the forthcoming FCA rules in relation to arrears and forbearance.

Question 8: Are stakeholders aware of any further consequential amendments that may arise from the disapplication of CCA information requirements?

N/A

Question 9: Do you have any comments on the proposed legislative approach to DMRs, credit broking and the Financial Promotions Order?

We have no real comments on the proposed approach except to say that, while we understand why the government does not wish for retailers to be brought within the new regime, BNPL is a form of embedded finance. The retail context has an influence on the impact on consumers using this form of credit. Retailers share responsibility for detriment in this market. Therefore, if the government does not want retailers to be caught by the new regime, the BNPL provider should ensure that the retailer promotes the credit in a fair and responsible manner.

We note that the consultation paper does not seem to ask a question in relation to sanctions at this point. We also disagree with the proposals to allow the sanctions set out in para 2.56 to fall away. We believe that while the majority of the day-to-day regulation of BNPL should be done under the forthcoming FCA regime, the existence of legal sanctions are also required to discipline the market.

Question 10: Do you have comments on the proposed legislation that seeks to implement the TPR?

We support the proposals regarding the implementation of the TPR. There is the obvious risk that currently unregulated BNPL will seek to exploit the period from now until regulation comes into effect. We will welcome a strong statement from the government and FCA that the market will be monitored closely and firms' behaviours during the period will be taken into account during the authorisation process.

Question 11: What do you expect the impacts to be of this proposed legislation on: providers of agreements that will be brought into regulation, consumers that use them and merchants that offer them as a payment option?

The impact on consumers will mostly depend on the FCA regime that implements the government's intention. As outlined above, if the particular type of detriment evident in the BNPL is to be addressed effectively then lessons should be learned from the payday lending market. Measures will be needed to constrain the activities of BNPL providers and to inject friction into the BNPL 'customer journey' to encourage consumers to consider their decisions.

Question 12: Do you agree with the provisional assessment that, on balance, the government's proposed proportionate approach to reform mitigates the negative impacts on those sharing particular protected characteristics and retain the positive equalities impacts of the products?

Again, this will very much depend on the FCA regime. We hope that the FCA, as part of any impact assessment, will undertake the type of evaluation it carried out in relation to the implementation of the payday lending regulations with additional focus on vulnerable consumers and those sharing protected characteristics.³ That evaluation demonstrated that even though the payday lending market was significantly reduced it actually enhanced consumer welfare. In other words, less is more. Given that consumers with protected characteristics are also more likely to be financially vulnerable, we would expect to see something similar with the BNPL market under a properly regulated regime.

Question 13: Do you have any further data you can provide on the potential impacts on persons sharing any of the protected characteristics?

Unfortunately, we do not have any further data.

**This marks the end of our submission.
November 2024**

³ [High-cost short-term credit | FCA](#)