Buy Now, Pay Later:
Consumer Protections Needed for the Popular New Way to Pay

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Introduction

Buy Now, Pay Later has emerged in recent years as an alternative form of credit, allowing consumers to split payments for a transaction and make smaller payments over time. In a challenged economy, with increasing interest rates and higher prices for retail goods, there is an obvious appeal to short-term credit that is potentially interest-free and allows lower up-front costs to consumers. Yet as this product continues to grow in popularity, are consumers meaningfully protected when using it?

In this paper, Consumer Reports seeks to highlight six key areas where users may experience gaps in consumer protection when using Buy Now, Pay Later (BNPL) loans. Our goal is both to alert consumers about potential risks and friction points in using these products when they shop, and to encourage the Consumer Financial Protection Bureau (CFPB) to quickly enact stronger consumer protections for this popular, rapidly growing form of payment.

The observations and recommendations that follow are guided in large part by responses to selected questions in CR's August 2022 nationally representative survey of 2,013 Americans who have used BNPL, as well as the September 2022 report issued by the CFPB about the risks and benefits of BNPL.

What is Buy Now, Pay Later?

Buy Now, Pay Later loans are a form of credit that allows a consumer to split the cost of retail transactions into smaller installments and take immediate possession of the product or service after making the first payment. Consumers typically pay a percentage of the asking price as a down payment at retail checkout counters or on websites, and enter into an agreement with the third-party financing provider to repay the balance of the loan by making a series of fixed installment payments over several weeks or months.

The most typical BNPL loans are the so-called "pay-in-four" products, where consumers pay 25 percent of the cost of the product or service at the time of sale, and the rest of the balance in three additional payments of 25 percent of the purchase price over the next six weeks, typically at 0 percent interest. Leading U.S. BNPL providers such as Afterpay, Affirm, Klarna, Sezzle, PayPal, and Zip all offer pay-in-four 0 percent interest BNPL loans.

The BNPL industry has grown rapidly in the U.S. over the past three years. The number of BNPL loans originated by five of the largest lenders grew by 970 percent from 2019 to 2021, from 16.8 million loans to 180 million loans, according to the CFPB. The value of the loans increased from $2 billion in 2019 to $24.2 billion in 2021. Industry analysts project high growth rates in the future, with some estimating that the global value of loans could reach over $1 trillion by 2030.[1]

[1] See also: GlobalData, *Buy Now Pay Later to Surpass $1 Trillion by 2030, GlobalData Says*, 10/28/22, available at: https://www.globaldata.com/media/thematic-research/buy-now-pay-later-surpass-1-trillion-2030-says-globaldata and https://www.globaldata.com/store/report/tech-in-2030-theme-analysis and Demos, Tellis. *Investors Seek Growth Now in Paying Later*, Wall Street Journal, 12/4/20, available at: https://www.wsj.com/articles/investors-seek-growth-now-in-paying-later-11607077800 citing Bank of America report projecting a $650 billion to $1 trillion market size by 2025.

BNPL loans are popular with many consumers because of their smaller payments and convenient repayment terms. They are also popular with retail and e-commerce merchants, who report larger average order sizes and an increased volume of return business. To obtain this increased revenue, retailers are willing to pay higher merchant fees to BNPL providers—of 6 to 7 percent, as compared with 1 to 3 percent for credit card sales.

As the volume of BNPL transactions has grown, consumer organizations and regulators have expressed concern that this new, popular payment method poses a variety of potential risks and friction points for users. These include the concerns that 1) users may become overextended by taking out too many loans at once; 2) consumers may have difficulties making returns and receiving refunds for goods that were returned; and 3) users may miss payments and incur late fees, interest charges, and overdraft fees, and have debts sent to collections, which can damage their credit standing.

Consumer Reports Coverage and Research on BNPL

As BNPL expanded in the U.S. over the past three years, Consumer Reports published a series of articles describing its growth and development and offering practical advice to consumers about how to use this emerging new payment method.[2] CR also collected stories from its members regarding their experiences with BNPL, and reviewed complaints to the CFPB and the Better Business Bureau.

In March 2022, CR submitted comments to the CFPB to express concern about some aspects of BNPL products and to highlight the need for stronger consumer protections, including better transparency for loan terms and fees, stronger ability-to-repay standards for loan underwriting, and better procedures for handling returns and payment disputes.[3]

In August 2022, CR conducted a nationally representative survey of BNPL users to learn more about consumer experiences with and opinions about BNPL. The survey was administered by SSRS via its

[2] Wang, Penelope. *The Hidden Risks of Buy Now, Pay Later Plans*, Consumer Reports, 2/21/21, https://www.consumerreports.org/shopping-retail/hidden-risks-of-buy-now-pay-later-plans-a7495893275; Picchi, Aimee. *What to Know About Buy Now, Pay Later Loans*, Consumer Reports, 5/30/19, https://www.consumerreports.org/loans/buy-now-pay-later-online-loans-what-to-know; Felton, Ryan. *The Trouble With Travel Loans*, Consumer Reports, 2/20/19, https://www.consumerreports.org/loans/the-trouble-with-travel-loans; Wang, Penelope. *How COVID Has Turned Buy Now, Pay Later Upside Down*, Consumer Reports, 2/20/21, https://www.consumerreports.org/shopping-retail/how-covid-has-turned-buy-now-pay-later-upside-down-a4434659796; Felton, Ryan. *I Bought a Burrito From Chiptole for Four Easy Payments,* Consumer Reports*,* 3/4/22, https://www.consumerreports.org/shopping-retail/the-downsides-of-expanding-buy-now-pay-later-plans-a2840564542.

[3] Bell, C. and Ejaz, S. *CR's Comments to the CFPB Regarding Buy Now Pay Later Providers*, Consumer Reports, 03/22/22, available at: https://advocacy.consumerreports.org/research/crs-formal-comments-to-the-cfpb-regarding-buy-now-pay-later-providers.

Opinion Panel of U.S. adults from Aug. 3 to 14, 2022. A sample of 2,013 U.S. adults completed the survey.[4]

The survey found, among other things, that:

- The percentage of Americans reporting that they have ever used a BNPL service surged in the seven months since we last asked about it, in January 2022,[5] rising 10 percentage points from 18 percent in January to 28 percent in August. And the percentage of Americans who said they had never heard of BNPL shrank from 32 percent in January to 17 percent in August.
- Black BNPL users were more likely than Hispanic or white BNPL users to have used BNPL at least six times: Forty percent of Black BNPL users had used it at least six times, compared with 29 percent of Hispanic BNPL users and 27 percent of white BNPL users. Also, Black BNPL users were more likely to say that they would definitely use BNPL again: Fifty-nine percent of Black BNPL users said they would definitely use it again, compared with 49 percent of Hispanic BNPL users and 37 percent of white BNPL users.[6]
- Sizable numbers of BNPL borrowers used it in risky ways: making their BNPL payments with a credit card (24 percent), making manual payments instead of automatic (29 percent), and having four or more concurrent BNPL purchases (10 percent).
- People with four or more concurrent purchases were twice as likely to have missed a payment than people with fewer concurrent purchases (18 percent of those with four or more concurrent purchases missed a payment, compared with 9 percent of those with fewer concurrent purchases).
- Missing a single payment was among the issues most commonly encountered by BNPL users, experienced by 7 percent of them, followed by unexpected fees or interest (6 percent), and having difficulty getting a refund for an item that was returned or never received (5 percent). Fully 50 percent of those who had missed at least one payment said it was because they expected to have the money but fell short.
- People with household incomes of $75,000 or more were more likely to say they've had no problems with a BNPL service—by about 13 percentage points, 82 percent compared with 69 percent, among those with household incomes under $75,000.
- Of those who missed one or more payments, 21 percent said their debt was sent to a collections agency, and 15 percent said the debt appeared on their credit report.

CFPB Efforts to Provide Stronger Oversight of BNPL

In December 2021, the CFPB issued a Request for Information to the industry and the public to obtain more specific information on the growth and activities of BNPL companies, and issues related to

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[4] August 2022 Consumer Reports nationally representative Buy Now Pay Later Services Survey of 2,013 U.S. adults, available at: https://advocacy.consumerreports.org/research/buy-now-pay-later-services-august-2022-nationally-representative-internet-survey.

[5] Consumer Reports nationally representative American Experiences Survey of 2,174 U.S. adults (January 2022), available at: https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_January_2022.

[6] Ibid.

accumulating debt, regulatory arbitrage, and data harvesting in the consumer credit market. The agency undertook the inquiry as part of its federal authority to monitor consumer financial markets, and to help make sure consumer financial products are safe and transparent for consumers.

In September 2022, the CFPB published the findings from its inquiry in a report titled "Buy Now, Pay Later: Market Trends and Consumer Impacts."[7] The report summarized data submitted by five of the largest BNPL providers, as well as comments and information received from other individuals and organizations, to provide an overview of the growing importance of BNPL in the marketplace, its impacts on consumers, and potential risks faced by consumers.

According to the report, BNPL loans have several substantive and competitive benefits over legacy credit products such as credit cards and charge accounts. These include financial benefits, such as no interest and no late fees for some products, and "operational" benefits, such as the fact that loans are widely available and easy to access and qualify for, and have a simple repayment structure.

However, the report also found that BNPL loans could pose "undesirable operational hurdles" for consumers, including the lack of clear disclosures of loan terms, could present challenges in filing and resolving disputes, and often require the use of auto-pay for all loan payments. The CFPB also expressed concern about potential violation of consumer privacy through data harvesting (i.e., lenders' use of consumer data to "deploy models, product features, and marketing campaigns based on that data to increase the likelihood of incremental sales"). Finally, the report noted that the BNPL business model may encourage credit overextension, either through "loan stacking," where users take out multiple loans within a short time frame, sometimes from different providers, or through "sustained usage," where frequent BNPL use over a period of months could interfere with users' ability to meet other budgetary needs, such as mortgage or car payments.

Who Uses BNPL Loans?

Consumer Reports' January 2022 nationally representative American Experiences Survey of 2,174 adults found that younger Americans were more likely to use BNPL than older adults. Over a quarter (26 percent) of 18- to 29-year-olds had used BNPL, along with 22 percent of 30- to 44-year-olds, 16 percent of 45- to 59-year-olds, and 10 percent of those 60 and older. Hispanic Americans (25 percent) and Black Americans (28 percent) were more likely to have ever used BNPL than white Americans (14 percent), according to that same survey.[8] In the August 2022 Consumer Reports survey, 59 percent of Black BNPL users said they would definitely use BNPL again, compared with 49 percent of Hispanic BNPL users and 37 percent of white BNPL users.[9]

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[7] Consumer Financial Protection Bureau. *Buy Now, Pay Later: Market Trends and Consumer Impacts*, September 2022, available at: https://www.consumerfinance.gov/data-research/research-reports/buy-now-pay-later-market-trends-and-consumer-impacts.

[8] Consumer Reports nationally representative American Experiences Survey of 2,174 U.S. adults (January 2022), available at: https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_BNPL_Only_January_2022.

[9] Consumer Reports 2022 BNPL Survey, p. 6.

According to a national survey by the Financial Health Network:

> … Financially Vulnerable households are nearly four times more likely to use BNPL than Financially Healthy households (18% vs. 5%). Additionally, 24% of households that reported using BNPL are considered Financially Vulnerable, compared with 13% of households that don't use BNPL.
>
> BNPL users are also more likely to struggle with credit. Nearly half of BNPL users (43%) report having subprime credit scores, compared with 24% of nonusers. Additionally, BNPL users who hold credit cards are more likely to have outstanding credit-card debt: 77% of BNPL users who also have credit cards say they have carried a balance on their credit cards over the past year, compared with 49% of nonusers. Interestingly, 23% of BNPL users and a similar percentage of nonusers (26%) do not use a credit card.[10]

Twenty-eight percent of BNPL users have household incomes of less than $30,000 per year, and 62 percent have incomes of less than $60,000, according to CR's January 2022 survey.[11] And according to CR's 2022 survey of BNPL users, people in lower-income households are more likely to have encountered a problem with a BNPL service, such as missing a payment or getting hit with unexpected fees or interest: Thirty-one percent of BNPL users with household incomes under $75,000 encountered a problem, compared with 18 percent of those with household incomes of $75,000 or more.[12]

Why Do Consumers Use BNPL?

By a considerable margin, the two most popular reasons for using BNPL are that it enables people to make a purchase they would not otherwise be able to afford (45 percent) and that people would rather pay in installments than in one lump sum (44 percent), according to the CR BNPL survey.[13]

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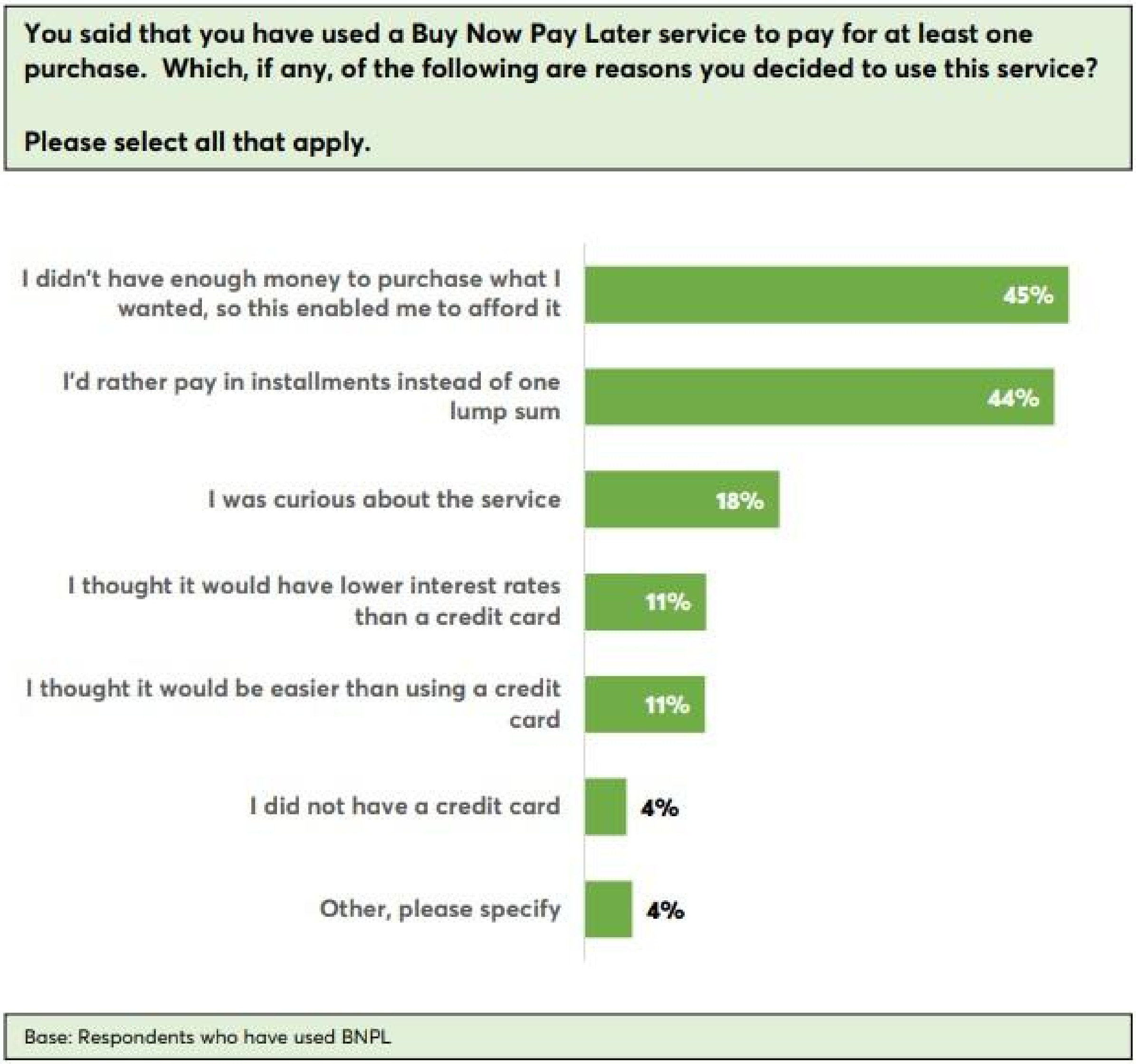
[10] Gdalman, Hannah, Greene, Meghan and Celik, Necati. *Buy Now Pay Later: Implications for Financial Health: A FinHealth Spend Product Spotlight*, Financial Health Network, March 2022, available at: https://finhealthnetwork.org/research/buy-now-pay-later-implications-for-financial-health, p. 6.

[11] Consumer Reports nationally representative American Experiences Survey of 2,174 U.S. adults (January 2022), available at: https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_January_2022.

[12] Consumer Reports 2022 BNPL Survey.

[13] Ibid., p. 8.



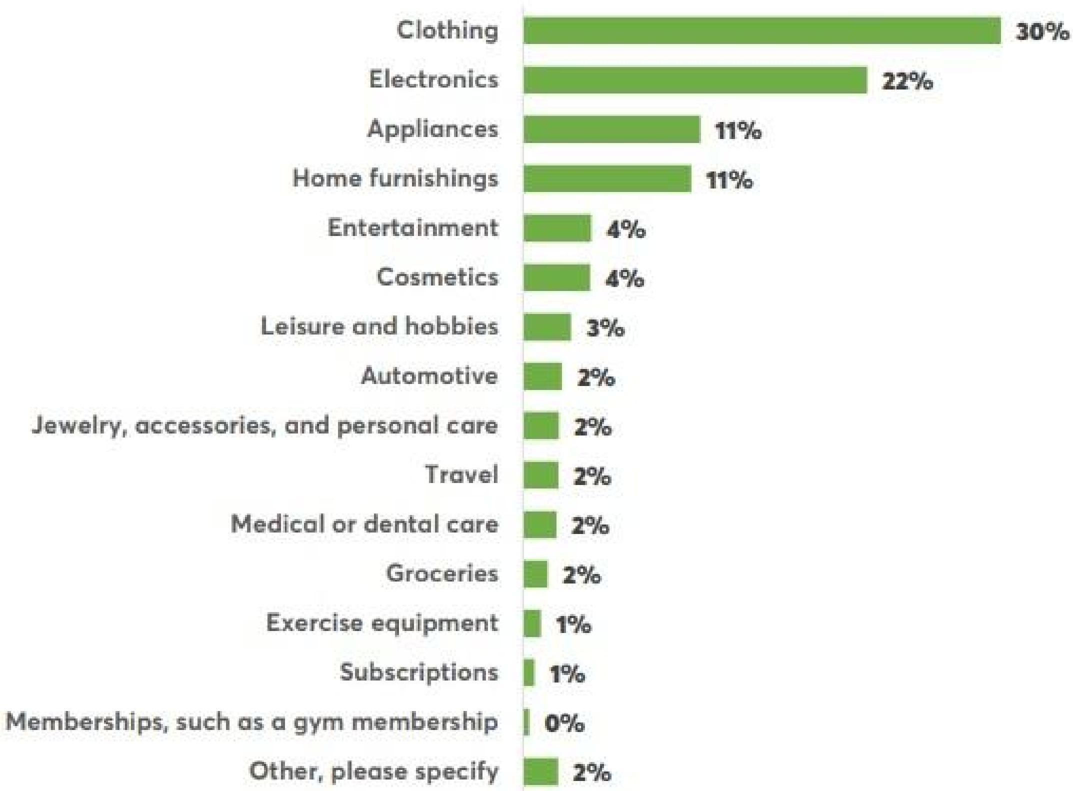
What Do Americans Buy With BNPL?

The most common purchases are clothing (30 percent) and electronics (22 percent), followed by appliances and home furnishings (11 percent each), according to the CR survey. Only a small number of people said their last BNPL purchase was for a repeated expense like groceries (2 percent) or a gym membership (less than 1 percent); this is particularly risky because the next bill might come before you've paid off the last one. Using BNPL for travel (2 percent) also poses risks, especially in the COVID-19 era, because making cancellations and adjustments can be more difficult with BNPL. The write-in responses in the "Other" category include gifts, pet supplies, firearms, education-related expenses, and utilities.[14]

[14] Consumer Reports 2022 BNPL Survey, p. 12.

What type of purchase was your last Buy Now Pay Later purchase?

Please select the category that is the best fit, even if it is not a perfect fit.



Base: Respondents who have used BNPL

6 Critical Gaps in Consumer Protections for BNPL Loans

From CR's reporting, survey research, and advocacy work, we have identified six areas where stronger consumer protections are urgently needed to ensure safe, transparent, and secure use of these products. As consumers expect to make significant use of BNPL during the 2022 holiday shopping season, they should be aware that these loans lack many of the consumer protections that come with other forms of credit.

GAP No. 1: BNPL loans don't always clearly disclose fees, interest rates, and payment terms.

Because of a gray area in federal law, it is unclear whether the most popular pay-in-four 0 percent BNPL loans are legally required to provide standardized cost-of-credit disclosures that are routinely required under the Truth in Lending Act (TILA) for credit cards and other types of consumer loans. While at least one BNPL lender provides these disclosures, most BNPL providers do not, according to the CFPB.[15] As noted by the CFPB:

> TILA, as implemented by Regulation Z, requires that lenders subject to its provisions provide consumers with a uniform set of clear and conspicuous cost-of-credit disclosures before consumers agree to take out a loan. Key information included in these [standardized] disclosures include, but is not limited to, the amount financed, total number of payments, finance charge and annual percentage rate, and potential late fee disclosures. … Regulation Z provides additional disclosure and other requirements that are specific to open-end credit, particularly to credit cards. These include, as applicable, requiring that account-opening disclosures disclose penalty rates, minimum interest charges, transaction charges, and grace periods, requiring periodic statements, and providing special credit card provisions such as consideration of the consumer's ability to pay …
>
> … The lack of clear standardized disclosure language may obscure the true nature of the product as credit and make important information about loan terms, including when and how fees are due, less accessible.[16]

Three national consumer organizations—the Center for Responsible Lending (CRL), Consumer Federation of America (CFA), and National Consumer Law Center (NCLC)—argued in their March 2022 comments to the CFPB that BNPL lenders are "Card Issuers" within the meaning of the Truth in Lending Act and should

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[15] Consumer Financial Protection Bureau. *Buy Now, Pay Later: Market Trends and Consumer Impacts*, September 2022, pp. 72-73, available at: https://www.consumerfinance.gov/data-research/research-reports/buy-now-pay-later-market-trends-and-consumer-impacts.

[16] Consumer Financial Protection Bureau. *Buy Now, Pay Later: Market Trends and Consumer Impacts*, September 2022, pp. 72-73, available at: https://www.consumerfinance.gov/data-research/research-reports/buy-now-pay-later-market-trends-and-consumer-impacts.

be required to make the same cost-of-credit disclosures that credit card companies are required to make under the Truth in Lending Act.[17]

Even if traditional disclosure requirements are strengthened, however, because of the proliferation of different BNPL products, and varying designs on websites and in digital apps, consumers may become confused about the terms of loans, repayment dates, and other product attributes, resulting in inappropriate product selection, and back-end fees and interest charges. Currently, BNPL products are not required to present the terms of the loans in a standardized format that enables consumers to easily find the information they need to understand how the loan works and to compare it with other options.

Further, because consumers are choosing BNPL loans at the retail or e-commerce point of sale, they are likely in a hurry to complete transactions. As a result, they may rapidly click through permission screens and overlook key information about how the loan works and its specific interest rates, fees, and other features.

Fees: CR's August 2022 survey found that 30 percent of respondents who used BNPL were unaware of at least one of the fees or other penalties for making late payments or missing payments when they used BNPL for the first time, compared with 70 percent who said they were aware of all the possible fees and other penalties.[18]

In addition to late fees, which are charged by most providers, some BNPL loans may charge fees that borrowers might not expect. For example, Zip charges an installment fee for taking out a loan with four payments. The fee varies by the amount of the BNPL loan taken out. The installment fee is $4 for purchases from $35 to $99.99, $5 for purchases from $100 to 199.99, and $6 for purchases $200 and above.[19] Sezzle charges a failed-payment fee when an electronic funds transfer fails; a convenience fee when a user uses a credit, debit, or prepaid benefits card to pay their installments; and a reschedule fee when more than one payment reschedule has been applied to a single order.[20]

The existence of various types of fees underscores the need to make sure that all fees are fairly disclosed at the outset of the transaction. Even where fees appear modest, because BNPL loans can be as short as six weeks, they may be large when translated into an annual percentage rate (APR). For example, the Zip website gives an example for a short-term $200 loan: "For a $200 purchase, you'd make four $51.50

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[17] Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers*, 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, pp. 29-36, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.

[18] Consumer Reports 2022 BNPL Survey, p. 19.

[19] Zip schedule of fees, accessed 11/16/22, available at: https://zip.co/us/how-it-works (bottom of page).

[20] Sezzle.com. Why was I charged a fee?, accessed 11/16/22, available at: https://shopper-help.sezzle.com/hc/en-us/articles/360046781511. See also: Sezzle User Agreement, available at: https://legal.sezzle.com/user.

payments every two weeks starting today for a 52.18 percent annual percentage rate and a total of payments of $206."[21]

National consumer advocacy groups have also expressed concern that late fees may function as hidden finance charges: "Some BNPL providers appear to have significant revenue from late fees. To the extent that late fees are used as a profit center, and BNPL providers are targeting consumers they know have a significant chance of paying late, these fees are essentially a finance charge, a hidden form of interest, that disguises the cost of credit," the consumer groups wrote in a joint publication.[22]

For this reason, the CFPB should review all fees charged and ensure that they are "reasonable and proportional" to the purpose the penalty or extra charge is assessed for, consistent with the provisions of the Credit Card Act provisions of the Truth in Lending Act, that governs late fees for credit cards.[23]

Interest rate charges: According to CR's survey, 28 percent of consumers with missed payments for BNPL loans said they were charged interest.[24]

Given the widespread public perception that most BNPL loans have 0 percent interest, this is a surprising result. While CR did not specifically ask whether consumers were aware of the interest rate for the product they used, the fact that a high percentage of users report being charged interest raises the concern that consumers may be entering into loan agreements without fully understanding the terms.

The CFPB has appropriately been focusing on how to improve disclosures for pay-in-four 0 percent products, because these are exempt from the TILA's disclosure requirements. However, it is also important to understand that consumers are routinely encountering other point-of-service loan products described and marketed as buy now, pay later that charge interest rates of up to 36 percent. While interest-bearing loans *are* required to make TILA disclosures, the proliferation of different BNPL products means that consumers may miss or overlook significant differences among the terms and fees of various products.

According to a report prepared by the credit report agency Equifax, "… BNPL actually encompasses many types of credit, including installment loans, credit lines, virtual rent-to-own models, and virtual focused larger ticket plays" (such as lending for medical expenses or home improvement costs).[25] For example, as part of their lending businesses, BNPL providers Affirm and Klarna also offer interest-bearing loans that may be described and perceived as BNPL products, with APRs of up to 36 percent and 28.99

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21 Zip schedule of fees, accessed 11/16/22, available at: https://zip.co/us/how-it-works (bottom of page).
22 Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers*, 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, p. 22, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.
23 Ibid., p. 37.
24 Consumer Reports 2022 BNPL Survey, p. 22.
25 *Buy Now, Pay Later: Sustaining Growth and Building Profitability*, Equifax, 6/8/22, available at: https://www.equifax.com/resource/-/asset/white-paper/bnpl-sustaining-growth-and-building-profitability.

percent, respectively. The BNPL travel lender Uplift charges APRs of up to 36 percent.[26] Thus, some BNPL loans can be as expensive as or even more expensive than financing the transaction on a credit card.

As the BNPL market grows, consumers should be able to quickly recognize and understand the difference between the pay-in-four 0 percent products and more expensive interest-bearing loan products. Consumers may switch between point-of-service loan products within BNPL company product families, or across BNPL companies, without fully realizing the differences between them. In stories received by CR, some consumers described certain products such as PayPal Credit as BNPL, when they are actually deferred-interest credit. Unless measures are taken to more clearly delineate among types of online loans, we expect this consumer confusion will continue to persist and grow.

Further, regulators should make sure that the BNPL disclosures are prominent and effective when presented on digital products such as computers, tablets, and smartphones. Even though interest-bearing loans are subject to hard credit checks and TILA disclosures, these disclosures made in their traditional form might not always be easy to see when you are checking out quickly online or using a payment app.

● PROTECTION: All types of BNPL loans should provide standardized, easy-to-understand disclosures regarding interest rates, fees, and payment terms.

The CFPB should require all BNPL products to provide standardized disclosures about loan terms, fees, and product features, so consumers can understand the products they are using and can anticipate what to do if they encounter problems.

In addition to information relating to the cost of credit, standardized disclosures should include a capsule summary of other important information that consumers need to know about BNPL loans, including:

- Whether the BNPL performs a soft or hard credit check;
- Procedures followed to report positive and/or negative information to credit bureaus;
- Notification that the BNPL provider is a separate company from the retailer or e-commerce merchant;
- How to contact BNPL customer service to arrange returns and refunds, and for other issues relating to payment and product use;
- Procedures followed by the BNPL to resolve disputes with merchants relating to quality of merchandise or nondelivery;
- Procedures followed by the company relating to missed payments and sending delinquent loans to debt collection; and
- Policies relating to data collection, security, and privacy.

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[26] Felton, Ryan. *The Trouble With Travel Loans*, Consumer Reports, 12/20/19, available at: https://www.consumerreports.org/loans/the-trouble-with-travel-loans. See also: https://www.uplift.com/, bottom of page, accessed 11/18/22.

While many or most BNPL companies provide this information somewhere on their websites or in their long user agreements, it needs to be prominently summarized so that consumers can more easily find it in one place.

Consumers should also have the right to receive periodic billing statements for BNPL loans, similar to what is required for credit cards. The CFPB should also clarify what type of billing statements should be provided by BNPL lenders. Currently, BNPL payment due dates fall on different days depending on when the purchase was made, which can lead to a confusing schedule of payments due when the consumer has more than one loan. The CFPB should study this issue and consider ways to ensure that fair statements and payment schedules can be synchronized in two-week intervals, so consumers will have an easier path to repayment, as proposed by the CRL, CFA, and NCLC.[27]

The CFPB should also consider conducting or requiring usability testing to ensure that the standardized BNPL disclosures will be effectively presented through digital means, so consumers are appropriately informed about product terms and features.

Disclosure will not solve or prevent all consumer problems related to BNPL loans, but it will improve fairness and transparency for key product terms and features, and help consumers better understand what they have a right to expect.

● CONSUMER ADVICE

As consumers wait for the CFPB to implement stronger consumer protections …

- Make sure you are aware of the specific interest rates, fees, credit reporting, debt collection, and privacy/security practices for the specific BNPL product(s) you are using.
- Recognize that there is substantial variation among products described and marketed as buy now, pay later and that not all such products are the same.
- Be especially careful to check interest rates and fees, so you understand how much you will be charged if you pay on time and/or miss a payment.

[27] Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers,* 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, pp. 38-39, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.

GAP No. 2: Consumers report problems with customer service when making returns and seeking refunds.

Many consumers have reported to the CFPB and Better Business Bureau that they have encountered difficulties making returns and receiving refunds for BNPL payments made for goods and services. And CR's August 2022 survey found that 5 percent of respondents who used BNPL reported that they had difficulty getting a refund for an item they had purchased or had never received. Four percent said they had difficulty stopping payments when they returned an item.[28] While these percentages may seem low, when they are extrapolated to the large base of people who are using BNPL loans, they represent a substantial number of users who may have difficulty making returns and getting refunds.

This problem may be less serious at larger retailers, which tend to have more staff assigned to help customers make returns and process refunds, while consumers who use BNPL with smaller companies or at less reputable websites may have a harder time getting the assistance they need.

This problem is often made more challenging because the customer must often contact customer service for both the retailer and the BNPL company, rather than just the retailer, to finalize a return.[29] In a 2021 article, Consumer Reports described the difficult return experience of one BNPL borrower:

> For L.T. Horhn, 48, a Los Angeles resident, obtaining a refund from Sezzle for a $200 handbag turned out to be a long ordeal.
>
> "I was shopping online last September and clicked—then I had second thoughts, since I didn't know the retailer," says Horhn.
>
> She tried to cancel the purchase, but she could not reach the retailer by phone, and Sezzle's customer representative told her that all requests must go through the merchant directly. Horhn sent back the bag, which was poor quality, she says. But the address given to her by the retailer turned out to be false, and the package was returned as undeliverable. Unable to get a refund

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[28] Consumer Reports 2022 BNPL Survey, p. 20. The results mirrored a similar January 2022 nationally representative survey of 2,174 U.S. adults carried out by Consumer Reports. Five percent of Americans who ever used BPNL services reported that they had difficulty getting into contact with customer service for the BPNL provider; and 4 percent reported that they had difficulty processing a return or refund specifically because they paid for the product with this service. See also: Wang, Penelope. *How COVID Has Turned Buy Now, Pay Later Upside Down*, Consumer Reports, 2/22/22, available at: https://www.consumerreports.org/shopping-retail/how-covid-has-turned-buy-now-pay-later-upsidedown-a4434659796 and Consumer Reports nationally representative American Experiences Survey of 2,174 U.S. adults (January 2022), available at: https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_BNPL_Only_January_2022.

[29] Bays, Ken. American Banker, *Buy Now/Pay Later Carries Myriad Challenges for Return Policies*, 03/17/21, available at: https://www.americanbanker.com/payments/opinion/buy-now-pay-later-carries-myriad-challenges-for-return-policies.

from Sezzle, she canceled payments through her bank, but the first one for $51 had already gone through.

Upon being contacted by Consumer Reports, Sezzle CEO Charlie Youakim reviewed Horhn's account, and she received a refund. Youakim also says Horhn should have initiated a dispute. Horhn responded that she did not understand where to do this on the website.[30]

Some consumers have also reported difficulties contacting customer service and getting timely responses when they are having a problem. In contrast to other payment methods, consumers using BNPL may have to contact both the merchant and the payment company, instead of just working with the merchant to process a refund payment. In the meantime, consumers can be left on the hook for making payments under the BNPL payment schedule for an item that they no longer want or that has already been returned.

Borrower challenges in making returns and receiving refunds are cited as a key issue in the CFPB report. According to the 2021 data collected by the CFPB, 13.7 percent of individual loans in 2021 had at least some portion of the order that was returned, up from 12.2 percent in 2020. And 60.3 percent of product returns and payment disputes were refunded to borrowers.

When seeking a return, the five BNPL lenders surveyed by the CFPB tell borrowers to contact the merchant that sold the product. If and when the merchant processes the return, the funds will be credited back to the borrower, after the BNPL provider has processed the refund.

According to the CFPB, the policies of the five BNPL providers for requiring continued payments during returns and payment disputes vary. "One lender surveyed requires continued payments pending a dispute, two lenders allow borrowers to defer payment for a short time following a reported dispute, and two lenders stop payment indefinitely during a reported dispute."[31]

As the CFPB explains, some returns result in payment disputes between consumers and merchants, where goods were not delivered or provided as agreed, or there are problems in communication as to whether the good was returned or not:

> The return process may be complicated when the merchant declines to authorize a refund for a disputed item. In these cases, a borrower may contact the BNPL lender to file a dispute, either via the lender's app or by contacting customer support. The BNPL lender then generally begins an investigation and contacts both the borrower and merchant. Once the investigation is concluded, the lender assigns responsibility to one party and may issue a refund or credit. However, with the short-term, six-week nature of BNPL loans, a successful merchant dispute may

[30] Wang, Penelope. The Hidden Risks of Buy Now, Pay Later Plans, Consumer Reports, 2/14/21, available at: https://www.consumerreports.org/shopping-retail/hidden-risks-of-buy-now-pay-later-plans-a7495893275.
[31] CFPB Report, p. 26.

not be resolved during the loan term. In these instances, the borrower may be required to make additional payments under the loan contract until the investigation is concluded.[32]

Additional problems processing returns arise from other types of BNPL transactions where the BNPL company has issued a single-use “virtual credit card” to fund a BNPL loan with a noncontracted merchant. These virtual cards permit use of BNPL financing at many outlets that likely do not even know the consumer is using a BNPL loan.[33]

The CFPB’s complaint database includes many complaints from consumers regarding protracted delays in making returns and obtaining refunds, and problems in communicating with customer service departments at merchants and BNPL providers.[34]

The Need for Chargeback Rights in BNPL Payment Disputes

Under the Fair Credit Billing Act (FCBA), credit cards and other “open end” revolving credit accounts provide “chargeback rights” for disputes with retailers when goods or services are defective, not delivered, or returned but not credited, or when charges are incorrectly billed in other ways. Chargeback rights allow consumers to withhold payment temporarily from their credit card company for the cost of the purchase and any finance charges for up to two billing cycles while the lender investigates the consumer’s complaint.

After receiving a billing statement, consumers have up to 60 days to contact the credit card company to notify them about the billing error. The credit card company then is required to acknowledge the potential error in writing, and must investigate and resolve the billing dispute within two billing cycles (but not more than 90 days) after receiving the consumer’s letter.[35]

Under the FCBA, consumers have the legal right to dispute billing errors including:

- unauthorized charges (federal law limits borrower responsibility for unauthorized charges to $50);
- charges that list the wrong date or amount;
- charges for goods and services that the borrower did not accept or that were not delivered as agreed;
- math errors;
- failure to post payments and other credits, such as returns;
- failure to send bills to the borrower’s current address—assuming the creditor has the borrower’s change of address, in writing, at least 20 days before the billing period ends; and

[32] CFPB Report, p. 25.
[33] Ibid.
[34] Ibid., p. 26 and CFPB Complaints related to Affirm, Afterpay, PayPal, Sezzle, and Zip.
[35] Federal Trade Commission, *Disputing Unfair Credit Card Charges*, available at: https://consumer.ftc.gov/articles/disputing-credit-card-charges.

- charges for which the borrower asks for an explanation or written proof of purchase, along with a claimed error or request for clarification.[36]

Chargeback rights are currently not required for BNPL loans, so consumers have fewer rights when they experience problems with nondelivery, fraud, or billing errors. Under the terms of their user agreements, BNPL lenders may provide some dispute resolution services, but they are not as robust as the rights provided under the FCBA.

The lack of chargeback rights is especially concerning when it comes to purchases of more expensive products such as appliances, exercise equipment, mattresses, and furniture; and travel services, where cancellations of flights, and hotel and cruise reservations, may put consumers at risk of losing large sums of money.[37]

● PROTECTION: Ensure fast, efficient resolution of issues relating to product returns and payment disputes.

The CFPB should promulgate specific standards and rules for ensuring fast and efficient resolution of returns and payment disputes for all BPNL providers, and monitor and collect data on lender performance in this critical area.

In addition, the CFPB and/or Congress should require chargeback rights for BNPL payment disputes so that consumers will have specific rights when they experience problems with nondelivery of products and services, receive poor-quality or defective merchandise, or incur billing errors as defined in the Fair Credit Billing Act. Consumers need fair, legally binding remedies when merchants fail to perform as promised. Providing chargeback rights will create a level playing field for different forms of credit and give consumers greater confidence when engaging in transactions that are funded through BNPL credit.[38]

● CONSUMER ADVICE

As consumers wait for the CFPB and/or Congress to implement stronger consumer protections …

- Be prepared to immediately contact both the retailer and the BNPL provider when you have to return an item, to make sure that the return is properly acknowledged and that you get prompt credit for any payments you've already made or that are coming due.

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[36] Ibid.

[37] Felton, Ryan. *The Trouble with Travel Loans*, Consumer Reports, 12/20/19, available at: https://www.consumerreports.org/loans/the-trouble-with-travel-loans.

[38] Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers*, 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, pp. 37-38, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.

- Ask the BNPL provider to reschedule your payment dates until the return/refund issue is resolved.
- Be aware that other consumers have experienced significant delays in receiving refunds for returned products. A return/refund in some situations could take weeks or even months. Make sure you have adequate funds in your bank or debit card account to keep making loan payments while any returns are processed. If you miss payments and a disputed loan is sent to collections, it could damage your credit standing.
- Be careful about making BNPL purchases from smaller websites and retailers you haven't interacted with before. They may have fewer staff members and less capacity to process returns quickly.
- Be prepared to file complaints with the CFPB at https://www.consumerfinance.gov/complaint or by calling 855-411-CFPB (855-411-2372) if the payment dispute or return issue has not been resolved. Financial services companies have to respond to complaints within 60 days, and the CFPB says many companies respond within 15 days. This is a good way to get a billing dispute resolved if merchants or BNPL lenders are giving you the runaround.

GAP No. 3: Consumers can find themselves overextended on credit and unable to keep up with payments.

In its report, the CFPB collected data that raises concerns that some BNPL providers may be overextending credit to borrowers who might not be able to pay back the loans. Because of gaps in the way that BNPL loans are originated and reported to credit bureaus, BNPL lenders do not have a full picture of how many loans their individual borrowers may have taken out from other BNPL companies. As a result, they may continue to offer loans to borrowers with multiple loans, who might not be able to pay them back.

This process is known as "loan stacking." While some borrowers can afford to pay for multiple loans, others are likely to run out of money when the payments are due, and incur multiple late fees and overdraft changes. If the borrowers fail to pay, their loans can be sent to debt collection. The delinquent loans can also potentially be reported to credit bureaus, and stay on the borrower's credit report for up to seven years.[39]

Five of the largest BNPL lenders revealed that 15.5 percent of borrowers took out five or more BPNL loans, and 4 percent took out 10 or more, during the last three months of 2021, according to data collected by the CFPB.[40]

CR's August 2022 survey suggests that loan stacking can be a risky practice for consumers. Respondents with four or more concurrent BNPL purchases were twice as likely to have missed a payment, compared with people who had fewer concurrent BNPL purchases (18 percent vs. 9 percent).[41]

This problem is related to two key challenges with BNPL products.

1) *Lack of ability-to-repay calculations in underwriting:* BNPL loans are typically issued without a full assessment of a consumer's credit status and ability to repay the loan. BNPL providers collect a borrower's name, e-mail address, and cell phone number, and usually do a soft credit check to determine eligibility for BNPL credit. While a BNPL loan functions in many ways similar to a credit card, usually less information is collected in BNPL applications than in typical applications for credit cards.

   This practice contributes to problems with loan stacking because, as mentioned above, it gives the provider only a partial picture of the consumer's ability to repay the loan. The lack of visibility into a consumer's ability to repay can create problems for BNPL providers themselves, as well as for other financial service providers, such as mortgage and auto lenders, that also use the credit reporting system.[42]

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[39] https://www.ftc.gov/business-guidance/resources/consumer-reports-what-information-furnishers-need-know.
[40] CFPB Report, p. 34.
[41] Consumer Reports 2022 BNPL Survey, p. 18.
[42] CFPB Report, p. 16.

Even if BNPL loans are made at 0 percent interest, without a formal determination and legal standard for the borrower's ability to repay, lenders may make loans for principal amounts alone (the cost of the item purchased) that could be difficult for consumers to repay. This can potentially create unreasonable risks for delinquency and default, which can lead to debt collection and damaged credit standing for borrowers.

2) *Credit assignment:* This term refers to how much you can borrow, for how long, and at what interest rate. Some consumers who have submitted complaints to the CFPB database have expressed concern about lack of transparency in how credit is assigned and provided by BNPL companies. Even though these borrowers think they are good customers, and have repaid their loans, the BNPL may deny them the ability to receive additional loans, or allocate them less credit than expected.[43]

According to the CFPB, "… Some consumers complained about arbitrary decreases, rendering them unable to use the product or make otherwise planned purchases: 'I've been having an account with [BNPL lender] for 2+ years and this is the 2nd time they dropped my limit and changed my status for no reason.' "[44]

BNPL credit assignment may also depend on the terms offered by specific merchants, who contract with the BNPL to generate business and "convert" more customers. Thus, the interest rates available for BNPL do not always reflect pure borrower creditworthiness but also depend on whether the retailer is willing, in effect, to subsidize the loan for the specific products it is selling.

Because BNPL providers do not generally perform hard credit checks and formally assess borrower ability to repay, however, their access to reliable data about an individual borrower's financial status is limited. In addition, because the protocols for reporting BNPL loans to credit bureaus are voluntary and underdeveloped, there is a lack of transparency which makes it impossible for any individual lender to accurately evaluate customer ability to repay.[45]

Consumers may also tap their credit capacity when they use credit cards to make payments on BNPL loans. CR's August 2022 survey found that 54 percent of respondents used debit cards to make payments, 27 percent paid directly from a bank or credit union account, and 24 percent of respondents made payments using a credit card. As CR survey researcher Noemi Altman commented, "Paying with a credit card can hold risks because it is essentially taking out one line of credit to pay another."[46]

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[43] CFPB Report, p. 20.
[44] CFPB Report, p. 20.
[45] Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers,* 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, pp. 17-21, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.
[46] Consumer Reports 2022 BNPL Survey, p. 15.

● PROTECTION: Establish fair standards for credit extension, so borrowers who pay on time can get additional loans at reasonable terms and maintain a good credit score.

The CFPB should require BNPL lenders to abide by an ability-to-repay standard to reduce risks of loan stacking and credit overextension, and provide fairer, more transparent credit assignment for consumers. Because BNPL companies typically approve a borrower for a credit amount up to a certain limit, they could be deemed by the CFPB to be similar to credit card providers. The advantage of this approach is that it would provide greater transparency into a borrower's actual financial standing so that lenders do not approve unsafe loans that borrowers can't afford to pay back. With a more accurate picture of a consumer's financial standing, the BNPL lender would have improved capacity to issue loans that track more closely with a borrower's creditworthiness, which could then be more effectively monitored by the CFPB.

● CONSUMER ADVICE

As consumers wait for the CFPB and/or Congress to implement stronger consumer protections …

- Be careful about taking out multiple BNPL loans. Keep track of all payment due dates. Make sure you have an adequate surplus of funds on your debit card or payment method to protect against missed payments and/or overdrafts.
- Avoid making payments on BNPL loans with credit cards, which increases the cost of borrowing and may create risks of incurring additional late fees and penalties from the credit card issuer. If you're struggling to keep up with your current bills, consider the possibility that your financial situation might not be better next month. Be careful about taking on more short-term loans that will come due before you know it.
- Maintain a household emergency fund equal to at least three months of income, to help provide a financial cushion in case you lose your job, your car breaks down, or you have unexpected medical expenses. If you have an emergency fund, you will have more financial capacity to stay on track with any BNPL payments you have.
- If you get behind on payments, understand that late payments can be reported to the credit bureaus and hurt your credit score. If your loan becomes delinquent, it may also be sent to debt collection.
- If you're shopping for holiday gifts, make a budget and stick to it. Generosity to friends and family is not a good reason to drive yourself deep into debt. Consider paying cash for gifts, because at least that way you know you won't be stuck with big bills to pay after the holidays.

GAP No. 4: Consumers can incur costly late fees and overdraft penalties.

BNPL loans are undoubtedly a great benefit for families that need access to credit and have the financial capacity and operational ability to pay them back on time. However, because BNPL is extensively used by people with modest incomes, borrowers may also be very close to the line of what they can actually afford. Because borrowers may take out multiple BNPL loans—and also may have other credit products they are using—there is a distinct possibility that many users could become overextended on credit obligations.

From the data collected from the five of the largest BNPL lenders, the CFPB found that 10.5 percent of unique users were charged at least one late fee in 2021, up from 7.9 percent in 2020. The CFPB also notes that consumers might be charged more than one late fee for a missed payment. The agency commented that:

> Late fees in the BNPL should be considered in the context of a product for which virtually all borrowers are on auto-pay. As a result, the assessment of a late fee suggests that a borrower's checking account lacked sufficient funds for the BNPL payment to be successful.[47]

Similarly, CR's survey found that 11 percent of respondents who used BNPL had missed one or more payments. Fully 50 percent of those who had missed a payment said it was because they expected to have the money but fell short. More than 1 in 3 (36 percent) of BNPL users who missed a payment said they had lost track of their payments and missed the deadline, and 16 percent thought they had set up automatic payment but the payment didn't go through.[48]

If borrowers can't afford the burden of repaying one or more BNPL loans, they may overdraw their bank accounts and debit cards. This can lead to expensive overdraft fees in addition to the BNPL late payment fees. Furthermore, overdraft fees may in turn result in borrowers being flagged by reporting agencies such as ChexSystems and Early Warning Services, which screen consumers on behalf of banks. That can make it more difficult for borrowers to get a bank account in the future.[49]

According to a January 2022 Morning Consult survey of 2,200 adults, users of BNPL services are much more likely to overdraw their bank or credit union accounts than the public at large. Thirty-three percent of BNPL users reported incurring an overdraft, compared with 15 percent of all adults.[50]

This high rate of overdrafting reinforces concerns that some BNPL users may have taken out too much credit, and remain at risk of regularly incurring late fees and overdraft fees when other bills and

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[47] CFPB Report, p. 24.
[48] Consumer Reports 2022 BNPL Survey, p. 22.
[49] Wu, Chi Chi. *Account Screening Consumer Reporting Agencies: A Banking Access Perspective*, National Consumer Law Center, October 2015, available at: https://www.nclc.org/resources/account-screening-consumer-reporting-agencies-a-banking-access-perspective.
[50] Williams, Claire. Morning Consult, *'Buy Now, Pay Later' Users Significantly More Likely to Overdraft Than Nonusers,'* 3/2/22, available at: https://morningconsult.com/2022/03/02/buy-now-pay-later-bnpl-overdraft-data.

household expenses come due. If BNPL companies were required to more fully assess borrower ability to repay, as discussed in the previous section, users would be less likely to miss payments and incur late fees.

The CR survey finding also raises concerns that consumers may have trouble ensuring that the automatic payment method will reliably work as expected. CR's survey report suggests that automatic payment is generally a safe and preferred practice for borrowers, to ensure that they are able to pay on time, protect their credit standing, and build their ability to receive additional BNPL loans. But it may also create a heightened risk of overdrafts for people who are living paycheck to paycheck. This CR survey finding bears repeating: *Fully 50 percent of those who had missed a payment said it was because they expected to have the money but fell short.*

The CFPB's report points out that the structure of BNPL loans has positive benefits. At the inception of the loan, the BNPL provider verifies that the consumer has the first 25 percent of the price of the purchase and a digital payment method to make the next three payments. There can be little doubt that without selecting an automatic payment method, many consumers could forget to make payments or choose not to pay. On the other hand, it can also be true that auto-payment creates increased risks of overdrafts and late fees for consumers.

Additionally, the CFPB expresses concern that the model of putting loan payments on automatic payment systems may contribute to risks for "sustained usage" of BNPL, "… in which frequent BNPL consumption over a period of months and years may affect consumers' ability to meet non-BNPL obligations."[51] Auto-payment may also impede consumer "agency" to change priorities of paying different types of bills. For example, if a consumer has a choice between paying a BNPL loan for three sweaters or defaulting on a mortgage payment, the borrower should prioritize the mortgage payment. Automatic payment systems may inhibit consumers from making that rational choice.

In general, federal law generally doesn't permit lenders to require automatic payments for other types of loans, and through various rules has tried to preserve consumer's rights for changing payment types and/or turning auto-pay off when needed. In our review of consumer stories about using BNPL, we noticed that consumers may also face challenges in changing payment methods if they are locked out of e-mail accounts or they lose access to bank funds because of identity theft.

Auto-payment may work very well for most people most of the time, but there may be a variety of extenuating circumstances where consumers may need more flexibility to change a payment method midstream.

● PROTECTION: Create stronger standards to prevent undue risk of incurring late fees and bank overdrafts.

[51] CFPB Report, p. 5, pp.66-69.

The CFPB should establish standards for ensuring that BNPL late fees are reasonable and proportionate to the cost incurred by lenders for a missed payment. The agency should prohibit charging multiple fees for the same missed payment.

The CFPB should also investigate ways to create better rules for how banks and financial institutions process BNPL overdrafts and so-called re-presentments, where the institution seeks payment again on the same day, potentially triggering additional overdraft fees. Similarly, BNPL providers and the CFPB should consider ways to provide borrowers with flexibility to substitute payment methods when needed, including in time-urgent situations where borrowers could miss the payment deadline.

This issue overlaps with two other protections on this list. If the CFPB can require BNPL lenders to adopt better underwriting practices and an ability-to-repay standard, the incidence of late fees would likely decline. Similarly, if BNPL lenders are required to make standardized disclosures of terms and fees, and to send periodic billing statements, consumers will have better up-front information to help them pay on time and avoid late fees.

● CONSUMER ADVICE

As consumers wait for the CFPB to implement stronger consumer protections …

- Make sure you know how much your BPNL charges for late fees, and plan to avoid them. Every additional fee you pay makes your original purchase more expensive.
- Keep track of all payment due dates. Make sure you have an adequate surplus of funds on your debit card or payment method to protect against missed payments and/or overdrafts. If you have multiple loans, use a spreadsheet or notebook to keep track of when payments are due.
- Make sure auto-pay is set up correctly. Check and recheck on your BNPL app or website to make sure the numbers for your debit card and/or bank account are entered correctly, and check back to make sure initial payments have gone through. Log in to your bank account shortly after the due dates to make sure payments are being sent on time to the BNPL provider.

GAP No. 5: BNPL lenders do not consistently report user payment history to credit bureaus.

According to the August 2022 Consumer Reports survey, consumers are not clear on how BNPL loans affect credit scores. One in 4 respondents said they are not sure how BNPL loans affect their credit score, and 21 percent believe BNPL loans have no effect on credit scores. Only 54 percent believe their credit score is currently being affected by BNPL loans.[52]

Consumers are understandably confused about how credit reporting bureaus handle positive and negative information about repayment of BNPL loans. Since the inception of BNPL, procedures for either checking the credit of borrowers or reporting on their use of the loans have been somewhat murky. Part of the reason for this is that some BNPL lenders positioned themselves as "payment plans" that were exempt from regulation and not a form of credit. In addition, hard credit checks and formal credit-card-like applications were not part of their business model. This low barrier to entry was an attractive feature for at least some users, who might not have qualified under stricter underwriting standards.

Similarly, with respect to credit reporting, BNPL lenders have given conflicting and inconsistent accounts of what information would be reported to credit bureaus. Some have previously stated that negative information would be reported, while a few have indicated that a positive history of repayment would help consumers build their credit score.

In addition, the three national credit reporting agencies (Equifax, Experian, and TransUnion) are still trying to develop methods to fairly reflect the status of these new short-term loans. Reporting BNPL payment histories to the credit bureaus is currently voluntary, and the bureaus have so far adopted differing methods for reflecting this information. One key problem is that because many BNPL loans only last six weeks and time frames for repayment are short, it is more challenging for the credit reporting agencies to show their use on a real-time basis because most creditors report on a monthly basis on accounts that are open for much longer periods of time.

As the CFPB explained in a June 2022 blog post:

> Until recently, few BNPL lenders furnished information about consumers to the nationwide consumer reporting companies (NCRCs). This lack of furnishing could have downstream effects on consumers and the credit reporting system. It could be bad for BNPL borrowers who pay on time and may be seeking to build credit, since they may not benefit from the impact that timely payments may have on credit reports and credit scores. It may also impact both BNPL lenders and non-BNPL lenders seeking to understand how much debt a prospective borrower is carrying.
>
> The CFPB believes that when BNPL payments are furnished it is important that lenders furnish both positive and negative data. We would also like to see the industry adopt standardized BNPL furnishing codes and formats appropriate to the unique characteristics of the product. Such standardization would in turn facilitate the consistent and accurate furnishing of BNPL payment

[52] Consumer Reports 2022 BNPL Survey, p. 24.

information. Furthermore, consumer reporting companies should incorporate the BNPL data into core credit files as soon as possible and ensure that BNPL data are accurately reflected on consumer reports. Finally, we'd expect scoring companies and lenders to build and calibrate models that account for BNPL loans' unique characteristics.[53]

Another potential gap in consumer knowledge is that borrowers might not be aware that late and missed BNPL payments will be turned over to debt collectors. Some companies, such as Afterpay, previously refrained from sending delinquent accounts to outside debt collectors, but the CFPB report indicates that the use of external debt collection companies is now common in the industry:

> … All five of the lenders surveyed have, at least some point between 2019 and 2021, used third party debt collectors to collect delinquent loan balances. Two of the lenders only used debt collectors for specific, short intervals, while the other three use debt collectors as part of their general collections strategy. One common industry practice is to refer loans to debt collectors after the loans have reached charged off status, and any payments made via debt collectors are usually counted in the lender's income statement as "recoveries." The third-party debt collector establishes a new relationship with the borrower. As a general practice, given the low-dollar, digital-first nature of the product, debt collectors collecting BNPL loans rely more heavily on digital communications channels (text and email) than on traditional channels such as phone calls and paper mail.[54]

The CFPB also notes that some consumers have submitted complaints indicating that their accounts were sent to collections for items they had already returned or that they were contacted by collection agencies for debts they had already repaid.[55]

Finding an effective solution will be challenging, however, for several reasons, as detailed by the CRL, CFA, and NCLC in their comments to CFPB.[56] First, BNPL loans serve many consumers who have subprime credit scores. If customers are turning to BNPL because they already have damaged credit, any mistakes they make in BPNL repayment may damage their credit standing even further.

Second, the credit reporting agencies are using divergent approaches to collecting and reporting the data. One bureau, Experian, is creating a specialty credit reporting bureau for BNPL accounts, similar to other specialty bureaus for particular types of subprime or nontraditional credit, while Equifax and

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[53] Kleinbard, Martin and Udis, Laura. *Buy Now, Pay Later and Credit Reporting*, 6/15/22, available at: https://www.consumerfinance.gov/about-us/blog/by-now-pay-later-and-credit-reporting.
[54] CFPB Report, p. 30.
[55] CFPB Report, p. 26. Note 46.
[56] Center for Responsible Lending, Consumer Federation of America, and National Consumer Law Center. *Notice and Request for Comment Regarding the CFPB's Inquiry Into Buy-Now-Pay-Later (BNPL) Providers,* 87 FR 3511, Docket No. CFPB-2022-0002, 3/25/22, pp. 17-21, available at: https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf. See also: Wu, Chi Chi. Buy Now, Pay Later Is Not a Cure for Credit Building, The Hill, 6/21/22, available at: https://thehill.com/opinion/finance/3529845-buy-now-pay-later-is-not-a-cure-for-credit-building.

TransUnion are including BNPL data in their main accounts and giving other lenders the option of looking at that data or not.[57]

Third, the way a positive history of repayment will be reflected will be heavily dependent on the credit scoring algorithms that are used. BNPL loans currently are reported as separate trade lines for each individual loan as a closed-end installment loan, rather than as a revolving line of credit. Because the loans are typically short-term, the standards for determining whether a payment is late are not clear, relative to other data that credit bureaus handle. However, if BNPL lenders were required to report on borrower use of an open-ended line of credit (e.g., the borrower is approved to use BNPL loans up to $2,500 over six months or a year), the reported data could more effectively summarize experience over a longer period of time and more easily fit into existing models, which penalize consumers for opening too many individual lines of credit.[58]

● PROTECTION: Establish industrywide standards for originating and reporting BNPL loans to credit bureaus.

While it may take some time to develop an effective credit reporting system for BNPL loans, the CFPB has a vital role to play in helping to create clearer rules of the road for how BNPL lenders can effectively and appropriately participate in the credit reporting system. The CFPB's role is critical because consumers have received conflicting information about how BNPL lenders use and report to the credit bureaus.

In addition to establishing industrywide standards for BNPL underwriting that guide how consumers become initially qualified for such loans, the CFPB should also establish standards for fair reporting of repayment history to credit reporting agencies. These standards can help prevent harm to borrowers with impaired credit who are more likely to use BNPL loans, and may potentially help consumers with low or no credit scores to build their scores over time. They can also help improve the accuracy and reliability of the credit reporting system as a go-to resource for other lenders.

● CONSUMER ADVICE

As consumers wait for the CFPB and providers to implement stronger consumer protections …

- Be aware that if you miss a payment or become delinquent on a BNPL loan, that information can be reported to credit bureaus and will likely affect your credit score.
- Check your credit report on a regular basis, to guard against unfair or inaccurate reporting by creditors. Go to www.annualcreditreport.com to order a free copy of your report from each of the three credit reporting agencies (Equifax, Experian, and TransUnion).
- Unpaid or disputed BNPL loans may be turned over to debt collectors. If you are engaged in a payment dispute, keep fighting and be highly vocal about your side of the story.
- File complaints with the CFPB if BNPL lenders and/or merchants are unresponsive.

[57] Ibid., p. 19.
[58] Ibid., pp. 20-21.

GAP No. 6: BNPL lenders collect personal data that may threaten consumer privacy and security.

In general, consumers expect BNPL lenders to observe strong data privacy and security standards, and to avoid overcollecting data that is not needed for the borrower's use of the product.

CR's August 2022 survey found that 2 out of 3 BNPL users (67 percent) believe it is extremely or somewhat likely that BNPL firms are sharing their personal information, while 17 percent think it is somewhat or extremely unlikely. Almost as many (16 percent) said they were not sure. Two out of 3 BNPL users (67 percent) said they are extremely or very concerned about their personal financial data being shared for commercial purposes, while 33 percent said they are not very concerned or not concerned at all.[59]

According to the CFPB's report, there are two main ways for BNPL lenders to acquire users:

1) *The merchant partner acquisition model:* Under this model, the BNPL lender contracts with specific online merchants to embed BNPL loan options on retailer checkout pages.
2) *The app-driven acquisition model:* Under this model, consumers complete applications on a BNPL-branded shopping app, and become "preapproved" to spend a certain amount of credit using a "virtual card," a temporary internet-issued credit card number. This allows the BNPL to be used with many more "nonpartnered merchants" who have not signed contracts, and also allows the BNPL to receive a portion of interchange fees from the transaction.

According to the CFPB, "The app-driven model further strengthens the consumer's relationship with the BNPL lender by driving the consumer to begin (and often end) their purchase journey within the lender's self-contained app ecosystem."[60] The use of the branded apps also has a variety of other business advantages for tracking user behavior, and testing approaches for driving greater frequency and volume of use, including extensive use of data analytics and possible dark patterns in the software that nudge users to make choices to buy certain products or take out additional loans.

The CFPB further said: "The practice of harvesting and monetizing consumer data across the payments and lending ecosystems may threaten consumers' privacy, security, and autonomy. It also may lead to a consolidation of market power in the hands of a few large tech platforms who own the largest volume of consumer data, [and] reduce long-term innovation, choice, and price competition."[61]

Consumers may think of the BPNL app as just a handy payment method, but it is more akin to a "pay to play" shopping mall. BNPL companies earn fees from retailers by promoting their products and referring customers to their stores and websites. Users may want to be aware of this important distinction so they can be in control of their buying decisions. Regulators should monitor the apps for possible "dark patterns" and data practices that are not in users' interests.

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[59] Consumer Reports 2022 BNPL Survey, p. 28.
[60] CFPB Report, pp. 75-76.
[61] Ibid.

According to a paper by Marshall Lux and Bryan Epps of the Harvard Kennedy School:

> Merchant perspectives, too, are wildly positive because merchants benefit significantly from the current business models of BNPL companies. BNPL is in many ways designed as more of a merchant product than as a consumer product. With convenient access at point-of-sale, particularly in online sales – BNPL products help drive merchant sales. RBC Capital Markets reported in 2021 that online BNPL "increases conversion rates 20-30% and lifts average ticket sales by 30-50%." BNPL impact on revenue for many merchants is definitely worth the fees.[62]

The risks to consumers of data harvesting and monetization could potentially contribute to sustained usage of BNPL loans and overuse of credit, fueled by merchant fees and marketplace pressures to boost sales for retail goods. Several surveys cited in the CFPB's report estimate the rate of "BNPL post-purchase regret" at between 20 and 50 percent of purchases. A nationally representative survey of 2,174 U.S. adults carried out by CR in January 2022 found that 9 percent of people who have ever used a BNPL service bought one or more products on impulse that they later regretted purchasing.[63] While consumers might be disappointed with purchases for a variety of reasons, the CFPB cites one study in particular that found that 32 percent of consumers had to "delay or skip paying an essential bill due to the payments on [their] Buy Now, Pay Later plans."[64] Media reports from other countries, such as Australia, which have more experience with BNPL, have reported similar findings for segments of BNPL users.[65]

There is undoubtedly a fine line to walk between achieving the substantial benefits of lower payments and convenience for BNPL loans, and preventing unfair uses of big data and predictive analytics that could induce overspending and accumulation of debt.

● PROTECTION: Create strong standards to protect consumer data privacy and security.

The CFPB and Congress should enact regulations and laws to protect consumer data privacy, and prevent unfair practices in digital financial products regarding data harvesting and "dark patterns" that induce consumers to make decisions against their own interests. They should also work to promote competition

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[62] Lux, Marshall and Epps, Bryan. *Grow Now, Regulate Later? Regulation Urgently Needed to Support Transparency and Sustainable Growth for Buy-Now, Pay-Later*," Harvard Kennedy School, Mossavar-Rahmani Center for Business and Government, M-RCBG Associate Working Paper Series No. 182, April 2022, available at: https://www.hks.harvard.edu/centers/mrcbg/publications/awp/awp182.

[63] Consumer Reports nationally representative American Experiences Survey of 2,174 U.S. adults (January 2022), available at: https://article.images.consumerreports.org/prod/content/dam/surveys/Consumer_Reports_AES_BNPL_Only_January_2022.

[64] CFPB Report, pp. 68-69.

[65] Blakkarly, Jarni. *Buy Now Pay Later: The Modern Day Debt Trap*, CHOICE, 6/15/21, available at: https://www.choice.com.au/money/credit-cards-and-loans/personal-loans/articles/is-buy-now-pay-later-a-modern-debt-trap. See also: CHOICE, *Global Alliance Calls for Regulation of Harmful Buy Now Pay Later Industry*, available at: https://www.choice.com.au/about-us/media-releases/2022/march/global-alliance-calls-for-regulation-of-harmful-buy-now-pay-later-industry.

and fair dealing by Big Tech platforms such as Apple, Facebook, and Google, which operate many of their own payment products.

● CONSUMER ADVICE

As consumers wait for the CFPB and providers to implement stronger consumer protections …

- Be aware that your BNPL app may serve you ads to encourage you to shop more frequently and take out additional BNPL loans. Remember to take your time and to carefully compare prices and product quality at other stores to make sure you are getting a good deal.
- Be careful about making impulsive purchases you may regret later on.
- There are a variety of limited steps you may be able to take to limit how BNPL companies collect data about your smartphone and web browsing habits. See the Federal Trade Commission's recommendations for how to protect your privacy online at https://consumer.ftc.gov/articles/how-protect-your-privacy-online.
- Data privacy protection is an area where consumer options to protect themselves are sharply limited by the lack of strong privacy laws. Join and support organizations like CR that are fighting for stronger digital rights.

Conclusion

According to CR's August 2022 survey, Americans feel quite positive about their BNPL experiences. A total of 86 percent of BNPL users said they were very satisfied or somewhat satisfied with BNPL, while 6 percent were somewhat dissatisfied and 3 percent were very dissatisfied. In addition, 88 percent of BNPL users said they will probably or definitely use it again.

However, as should be clear from this report, BNPL loans also have risks and problematic features that consumers might not fully recognize or understand. In addition, consumers may use BNPL in risky ways, for example, by taking multiple loans out at once, missing payments and incurring late fees, and paying for loans by using credit cards.

Taken together, the six gaps in consumer protection described above are highly concerning because they represent the rough edges of a marketplace that is only now coming into public focus. As consumers continue to use BNPL, they may run into a variety of challenges and unexpected outcomes because these products have fewer protections than similar products such as credit cards and charge cards. While consumers can take certain steps to guard against particular risks, ultimately stronger public policies and marketplace protections must be put into place to create enduring, reliable protections that are available to all customers.

Through its September 2022 report, the CFPB has helped to clearly define the issues that must be addressed and clarified, to help assure that consumers can use BNPL loans safely. We urge the agency to continue its efforts to put stronger protections in place. The CFPB should use its authority under the Dodd-Frank Act to supervise BNPL providers by issuing a regulation defining the "larger participants" in the BNPL market. Further, the agency should require BNPL providers to provide comparable protections to credit cards for the key issues discussed in this report, such as cost-of-credit disclosures, ability-to-repay standards, periodic billing statements, chargeback protections, and better, clear procedures for credit reporting. These protections not only make common sense but also will help borrowers to use BNPL loans more wisely and safely, and eventually reduce the burdens on lenders, merchants, and government agencies that handle disputes and complaints.

As consumers shop for gifts this holiday season, many will take out BNPL loans that have inadequate and spotty protections. We hope that 2023 will be a year where we can put some or all of the gaps discussed in this report fully behind us. Until then, we urge BNPL users to be careful about the challenges and risks discussed in this report and to be prepared to speak out and seek help if things go wrong.