



Buy Now, Pay Later

Policy Measures to Mitigate Consumer Risks
from Evolving Business Practices

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Table of Contents

Executive Summary	3
I. Introduction	6
II. Current Trends in the BNPL Market	7
Key features of ‘traditional’ BNPL products	7
Expansion to longer-term, interest-bearing loans	8
Shifts toward app-driven acquisition models	9
III. Consumer Use of BNPL	12
Main uses of BNPL and levels of usage	12
Characteristics of BNPL users	13
Consumer motivations for using BNPL	15
IV. Problematic Practices of BNPL Providers	16
Wide variance and poor transparency in pricing structures	17
Multiple and excessive fees	19
Automatic repayments and use of credit cards for repayment	21
Limited assessment of repayment capacity	22
Inconsistent credit reporting	22
Exploitation of behavioral biases	23
Data harvesting and data privacy	24
Challenges with returns	26
V. Broader Potential Harms to Consumers	27
Overindebtedness	28
Overspending	29
VI. Policy Measures to Mitigate BNPL Risks to Consumers	30
Enhanced disclosure and transparency	31
Responsible lending	32
Credit reporting	33
Fair marketing	33
Stronger data privacy	34
Improved dispute resolution	35
Additional measures	35
Mechanisms for implementing recommendations	36
Acknowledgements	38

Executive Summary

“Buy Now, Pay Later” (BNPL) is an innovative credit product that has experienced rapid growth in the past few years. BNPL allows consumers to split up the cost of a retail transaction (usually between \$50 and \$1,000), traditionally into four interest-free installments repaid over the span of six weeks. Seamlessly integrated into the online shopping experience, the product is promoted as a fast, convenient means for consumers to manage their cash flow and avoid high-cost debt.

Unfortunately, the “free and seamless” nature of BNPL can be a double-edged sword. As of December 2022, 21% of Americans reported having used a BNPL service.¹ Many consumers express a positive view of BNPL, in particular appreciating the ability to spread out payments with no interest. However, research shows that BNPL users are typically worse off financially than non-users,² and the top reason BNPL users cite for using BNPL is to make a purchase that they could not afford otherwise.³ The data suggests that while some consumers are indeed benefitting from BNPL, others are using BNPL in a manner harmful to their financial well-being.

In addition, BNPL providers employ a range of practices that pose risks to consumers. This includes using confusing pricing and fee structures, imposing multiple and excessive late fees, requiring automatic repayment of BNPL loans, and in some instances allowing consumers to use credit cards for repayment. An increasing number of BNPL providers are now offering “BNPL” products that come with interest, potentially creating confusion for consumers. These practices can result in consumers incurring relatively significant costs for what is touted as an ostensibly “free” product.

BNPL providers also do not typically conduct a full assessment of an applicant’s ability to repay a loan, nor do they consistently report repayment information to credit bureaus. As a result, customers are at risk of overextension and overindebtedness. In fact, one survey cited by the Federal Reserve Bank of Kansas City found that 26% of BNPL users have missed making payments on BNPL loans,⁴ with financially

¹ Consumer Reports nationally representative American Experiences Survey of 2,017 U.S. adults (December 2022), article.images.consumerreports.org/image/upload/v1672847923/prod/content/dam/surveys/Consumer_Reports_AES_December_2022.pdf.

² Consumer Financial Protection Bureau, “Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey,” March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

³ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁴ Piplsay survey of 31,000 U.S. consumers from September 2020-September 2021. Cited in Julian Alcazar and Terri Bradford, “The Appeal and Proliferation of Buy Now, Pay Later: Consumer and Merchant Perspectives,” Federal Reserve Bank of Kansas City, November 2021, www.kansascityfed.org/research/payments-system-research-briefings/the-appeal-and-proliferation-of-buy-now-pay-later-consumer-and-merchant-perspectives.

vulnerable consumers three times as likely as overall users to report difficulty in making payments.⁵ One survey found that 32% of respondents had to “delay or skip paying an essential bill due to the payments on [their] Buy Now Pay Later plans.”⁶

Some BNPL providers have recently shifted to providing a full-service online shopping experience, moving away from BNPL being offered at checkout as a one-time service. This shift has changed the dynamic between BNPL providers and consumers in a manner that introduces new risks for consumers. BNPL providers have begun utilizing data harvesting to develop targeted, personalized content and leveraging deceptive designs in the digital user experience (UX). Such techniques are designed to increase customer conversion and incremental spending and have been shown to be quite successful in leading consumers to overspend. A 2022 Financial Health Network survey found that 30% of BNPL users reported having spent more than they would have if BNPL was not available, while 34% of BNPL users said they would not have made the purchase at all if the BNPL option had not been available.⁷ Given that many BNPL users are already financially strained, these incidences of overspending are concerning.

BNPL currently falls within a legal gray area, with few specific rules that apply to the product. As a result, consumers have little protection from the practices that may cause them harm. In particular, the subset of consumers using BNPL more for lending purposes as opposed to a convenient payment method are not protected by common safeguards for lending. This report suggests that policymakers develop a nuanced, proportionate regulatory approach for BNPL that preserves the benefits and innovative nature of BNPL while addressing the real risks and harms that BNPL can cause to certain users. In some instances, existing rules can be extended to BNPL, while in other instances tailored approaches may need to be developed.

Policy measures that are recommended to mitigate BNPL risks to consumers include the following:

- Enhancing disclosure and transparency, in particular making clearer distinctions between interest-free and interest-bearing loans and developing a standardized format for disclosing product features and pricing.
- Requiring BNPL providers to assess a consumer’s ability to repay, with potential exceptions for the smallest BNPL loans offered via blind “lend-to-learn” models and putting in place other responsible lending measures.
- Requiring BNPL providers to report to credit bureaus and developing an appropriate approach for how to treat BNPL data.
- Establishing stronger data privacy measures, particularly on the collection, use, and sharing of data.
- Extending chargeback rights for credit cards to ensure that BNPL users have clear rights with respect to dispute resolution.

⁵ Hannah Gdalmán, Meghan Greene, and Necati Celik, “Buy Now, Pay Later: Implications for Financial Health,” Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

⁶ “Survey: Buy Now Pay Later Plans Fuel Debt Struggles,” DebtHammer nationally representative survey of 1,050 U.S. buy now, pay later plan users (February 2022), debthammer.org/buy-now-pay-later-survey.

⁷ Hannah Gdalmán, Meghan Greene, and Necati Celik, “Buy Now, Pay Later: Implications for Financial Health,” Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

The BNPL industry can also play an important role in raising the standards across the market. Some BNPL providers have already begun to introduce more responsible practices, and this trend should be continued.

I. Introduction

“Buy Now, Pay Later” (BNPL) products are a new form of credit that enables consumers to split up the cost of a retail transaction, typically into four interest-free installments paid over the span of six weeks. Often integrated into the online shopping experience, BNPL offers a convenient and low-cost payment method to consumers compared with credit cards and traditional installment loans. As a result, the BNPL market has grown dramatically in recent years. From 2019 through 2021, the number of BNPL loans originated in the U.S. by five major lenders (Affirm, Afterpay, Klarna, PayPal, and Zip) grew more than tenfold, from 16.8 million to 180 million.^{8,9}

The rapid growth and popularity of BNPL have also raised some concerns. While BNPL products provide financial benefits and convenience, these benefits also pose a double-edged sword. Ease-of-use and ubiquity can lead to a range of risks for consumers, including overindebtedness, overspending, harm to credit scores, and data privacy concerns. At the same time, existing financial consumer protection legal and regulatory frameworks are not designed to adequately cover the risks arising from these new types of products and lenders.

This report highlights recent trends in the BNPL market, examines the practices of BNPL providers that pose risks to consumers, and suggests a range of approaches to mitigate these risks. The suggestions are intended to help inform policymakers seeking to issue guidance or rules on BNPL, such as the Consumer Financial Protection Bureau (CFPB). The suggestions can also be employed by the industry to raise its own standards and practices. The ultimate objective is to contribute to the development of a digital finance marketplace that is fair and inclusive, and delivers positive outcomes for consumers.

The report draws from existing research and literature, in particular recent research conducted on BNPL by Consumer Reports (CR). As part of its ongoing Digital Finance Initiative, CR tested and rated a representative group of BNPL apps to uncover how the apps perform relative to the Safety, Privacy, and Transparency Principles of the Fair Digital Finance Framework,¹⁰ and also conducted demand-side research to gather insights on consumers’ experiences with BNPL.¹¹ While the primary focus of the report is on “traditional” pay-in-four, interest-free BNPL products, the report also addresses the fact that many BNPL lenders are now offering longer term, interest-bearing products under the same “BNPL” umbrella term, creating confusion for some consumers.

⁸ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁹ Note that statistics from this report cover only the five noted BNPL providers and only “pay-in-four,” interest-free BNPL loans. Other sources cited in this report, particularly demand-side data, may encompass a broader conception of BNPL loans. The lack of a clear definition of BNPL creates challenges in tracking and comparing data on the industry.

¹⁰ Consumer Reports Fair Digital Finance Framework, advocacy.consumerreports.org/issue/money/financial-fairness.

¹¹ Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

II. Current Trends in the BNPL Market

At the outset, it is important to note that the BNPL market is currently in a state of flux along multiple dimensions. New types of providers have entered the market, new types of BNPL products are being offered, and new business models are being utilized to reach more consumers. Depending on the provider, BNPL may be pitched as a payment tool, a loan product, or a service to consumers. The shifting dynamics of the BNPL industry have introduced new types of risks for consumers and will have implications when designing appropriate policy approaches.

The BNPL market was initially comprised primarily of fintech companies, including Affirm, Afterpay, Klarna, PayPal, Sezzle, and Zip. However, other actors have now joined the broader BNPL ecosystem. Fintechs have formed partnerships with, or been acquired by, banks, card issuers, payment companies, and Big Tech companies in order to achieve greater reach and offer a broader range of services.¹² Mastercard and Visa have both introduced services designed to make it easier for companies to scale BNPL products, including virtual cards and Mastercard Installments and Visa Installments.¹³ Some banks have piloted BNPL products of their own, as have Big Tech companies such as Apple.¹⁴

As noted previously, the BNPL industry has experienced exponential growth, particularly during the early stages of the COVID-19 pandemic. From 2019 to 2021, the number of BNPL loans originated in the U.S. by five BNPL lenders surveyed by the CFPB grew by 970%, from 16.8 million to 180 million. The dollar volume of these originations grew 1,092%, from \$2 billion to \$24.2 billion.¹⁵ BNPL accounted for 5% of North American e-commerce transactions in 2022 and is projected to grow to 7% by 2026.¹⁶ However, recent macroeconomic conditions including high inflation and increasing costs of financing, combined with increasing BNPL delinquencies, may dampen the growth trajectory of the industry while also compelling BNPL providers to diversify their revenue streams.

Key features of ‘traditional’ BNPL products

For purposes of this report, “traditional” BNPL products are defined as pay-in-four, interest-free installment loan products. Traditional BNPL products typically share the following features, though even among traditional products there can be significant variance in how these features are structured:

- The typical BNPL product divides a \$50 to \$1,000 purchase into four equal installments.

¹² For example, Affirm partnered with Amazon in August 2021, Klarna entered into a partnership with Stripe in October 2021, and Square acquired Afterpay in February 2022.

¹³ Mastercard Installments and Visa Installments allow issuers to extend BNPL loans to existing credit card customers through online bank portals and also allow merchants to offer installment solutions at the point-of-sale.

¹⁴ Apple launched Apple Pay Later in March 2023.

¹⁵ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf. The CFPB report includes data from Affirm, Afterpay, Klarna, PayPal, and Zip and covers only traditional “pay-in-four” products.

¹⁶ Worldpay from FIS, “GPR 2023: The Global Payments Report,” 8th edition (2023), www.fisglobal.com/en/global-payments-report.

- In 2021, the average purchase amount financed by a traditional BNPL loan was \$135.¹⁷ Average loan sizes vary by BNPL provider; Afterpay and Klarna transactions are typically under \$250 and average around \$100, while Affirm transactions average around \$800.¹⁸
- In terms of repayment, the first installment is made as a down payment at checkout, while the remaining three payments are due in two-week intervals over a period of six weeks.
- Borrowers are typically required to use an existing debit or credit card for the initial down payment, which is then used for automatic debits for the remaining three payments. In 2021, 89% of installments payments were made via debit card, while 10% were made via credit card.¹⁹
- When assessing a prospective customer, BNPL providers often rely on information obtained via a “soft” credit check, in addition to a consumer’s purchase and repayment history with the company. Soft credit checks do not impact a consumer’s credit score, adding to the ease and convenience of BNPL.
- Unlike traditional installment loans, the product typically does not include any interest or upfront fees (though larger BNPL loans come with interest).
- Many BNPL lenders charge late fees or interest for missed payments. In 2021, 10.5% of borrowers were charged at least one late fee, an increase from 7.8% in 2020.²⁰ Policies toward late fees vary significantly, as described further below.

Expansion to longer-term, interest-bearing loans

While the BNPL market is predominantly still made up of traditional BNPL loans, many providers have begun to offer a broader range of installment loan products. CR’s research found that 4 out of 7 BNPL providers provided payment plan options beyond the traditional pay-in-four.²¹ These installment financing options have larger loan sizes, longer time horizons, and in some instances come with interest

¹⁷ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

¹⁸ Marco Di Maggio, Emily Williams, and Justin Katz, “Buy Now, Pay Later Credit: User Characteristics and Effects on Spending Patterns,” National Bureau of Economic Research, Working Paper 30508, September 2022, www.nber.org/papers/w30508.

¹⁹ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

²⁰ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

²¹ Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

rates that can match or exceed the average rate for credit cards. For example, Affirm reportedly offers loans of up to \$25,000²² with annual percentage rates (APRs) of up to 36%²³ (compared with 20.9% for credit cards),²⁴ while Sezzle offers loan terms up to 48 months (via a third-party lender).²⁵ As noted by the Federal Reserve Bank of Philadelphia:

“Indeed, the main product advertised on Affirm’s website as of March 2022 is a three- to 12-month traditional installment loan, and PayPal (whose BillMeLater product was an early version of BNPL and is now known as Pay in 4) offers a wide variety of traditional credit products.”²⁶

Data on the breakdown of the BNPL market is lacking, further hampered by the lack of a consistent definition and understanding of what falls under the term “BNPL.” However, a 2022 survey by the Financial Health Network found that:²⁷

- 10% of households in America used BNPL in the 12 months prior to November 2021.
- 70% of these households used a service that offered short-term financing with no interest.
- 21% used a longer-term, no-interest model.
- 11% used a BNPL service that applied interest.

These statistics suggest that a not insignificant percentage of consumers are using longer-term and interest-bearing BNPL products, and this trend is likely to continue, given increasing pressures on the market.

While this trend in itself is not necessarily problematic, there are indications that some consumers are confused or misled by the fact that some BNPL products come with interest. Marketing for BNPL has long heavily emphasized the “free” nature of the product, yet the reality is a broader range of products are now being offered that include interest and also involve a hard credit check, both aspects that may come as a surprise to consumers. In fact, research by CR found instances of consumers signing up for a BNPL loan that they expected to be interest-free, only to find out later that they would be charged interest.²⁸

Shifts toward app-driven acquisition models

²² Cheyenne DeVon, “Apple just launched its own buy now, pay later service—here’s how it compares with Affirm, Afterpay, Klarna and PayPal,” *CNBC Make It*, updated April 6, 2023, www.cnn.com/2023/03/30/how-apple-pay-later-compares-with-affirm-afterpay-klarna-paypal.html.

²³ Affirm, www.affirm.com/business/apr-calculator.

²⁴ Average interest rate for credit card accounts that assess interest in first quarter 2023. See Federal Reserve Board, www.federalreserve.gov/releases/g19/current.

²⁵ Sezzle, sezzle.com.

²⁶ Tom Akana, “Buy Now, Pay Later: Survey Evidence of Consumer Adoption and Attitudes,” Federal Reserve Bank of Philadelphia, June 2022, www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/discussion-papers/dp22-02.pdf.

²⁷ Hannah Gdalmann, Meghan Greene, and Necati Celik, “Buy Now, Pay Later: Implications for Financial Health,” Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

²⁸ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

In addition to expanding to traditional installment loans, the other major trend observed in the BNPL industry that has implications for consumers and policymakers is the shift toward the so-called “app-based acquisition model.” BNPL providers originally relied on the “merchant acquisition model,” forming direct relationships with individual merchants who present BNPL as a payment option at checkout. Under this model, merchants are charged a fee for each loan resulting in a sale.

Due to shrinking unit margins caused by decreases in revenue from merchant fees as well as increases in credit losses,²⁹ combined with increasing financing costs, there has been a noticeable shift to an app-driven acquisition model.³⁰ Under this model, BNPL providers pre-approve shoppers for credit before the point-of-sale from within the BNPL provider’s app or website, much like a short-term line of credit.³¹ Consumers can then use the app or website to shop around for products from various brands. Affirm, Afterpay, Klarna, and Sezzle now all have in-app and online experiences that function like online shopping malls.

The app-driven acquisition model can be viewed as part of the broader trend of BNPL increasingly being integrated into platforms that provide a full-service shopping experience rather than a one-off product or service. For example, Klarna introduced a range of complementary features in April 2023, including a personal shopping assistant that provides real-time advice and product recommendations and an AI-powered discovery shopping feed that helps consumers find items most relevant to them based on their preferences.³² A Klarna executive stated that “*candidly, ‘buy now, pay later’ is just a feature*”³³ of a broader offering.

While an app-driven acquisition model is not necessarily more or less dangerous to consumers, the new model changes the nature of the relationship and the dynamics between BNPL providers and consumers in a manner that introduces new types of risks to consumers. Under this model, providers receive referral fees (or affiliate fees) paid by merchants to BNPL providers for driving traffic and sales. BNPL providers are therefore incentivized to maximize stickiness to create a tighter ongoing relationship with customers. Several BNPL lenders have developed loyalty and reward programs to make the shopping experience more fun and rewarding. BNPL providers may also be inclined to use deceptive designs in

²⁹ Unit margins, i.e., how much a lender makes or loses for every \$100 of loans originated net of expenses, decreased from 1.27 to 1.01 from 2020 to 2021. See Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

³⁰ Share of revenue from non-partnered merchants, which can serve as a rough proxy for use of the app-based acquisition model, doubled from 11% in 2019 to 19-22% in 2021. See Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

³¹ BNPL providers refer to the pre-approved amount using a variety of terms, including “purchase power,” “pre-approved to spend,” “estimated spending power,” and “prequalified to spend.” See Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

³² Klarna, www.klarna.com/uk/business/marketing-solutions/virtual-shopping-for-business.

³³ James Ledbetter, “‘Buy Now, Pay Later’ Is the Victim of its Own Success,” *The New York Times*, January 28, 2023, <https://www.nytimes.com/2023/01/28/business/dealbook/buy-now-pay-later-struggles.html>.

designing user interfaces and experiences that lead consumers to transact more and habitually use BNPL, potentially leading to overspending and overextension.

The new business model also provides BNPL providers with “copious eyeballs, dollars, and data flow as a result.”³⁴ BNPL providers may seek to monetize data on consumers and their behavioral patterns and offer data-driven services to brands, including targeted ads, personalized content, and customer profiles. Such practices raise potential risks to consumers related to data privacy as well as overspending, which are further discussed in Sections IV and V.

³⁴ Esmé E. Deprez, Evan Weinberger, and Jennifer Surane, “The Buy Now, Pay Later Juggernaut Is About to Be Tested,” *Bloomberg Businessweek*, July 28, 2022, www.bloomberg.com/news/features/2022-07-28/klarna-affirm-afterpay-face-scrutiny-over-credit-business#xj4y7vzkg.

III. Consumer Use of BNPL

Main uses of BNPL and levels of usage

BNPL use was originally concentrated in the beauty and apparel industry but has diversified to other industries in recent years. Beauty and apparel merchants previously constituted 80.1% of origination in 2019, which decreased to 58.6% in 2021.³⁵ Over the same time period, BNPL use increased in areas such as electronics, fitness/sporting equipment, games/hobbies, jewelry, department stores, and general goods and merchandise. A 2022 nationally representative consumer survey by CR found clothing, electronics, appliances, and home furnishings to be the top four categories of purchases by BNPL users.³⁶

While use of BNPL for everyday necessities such as transportation, groceries, food, and utilities remained relatively low at 0.9% of Gross Merchandise Volume (GMV)³⁷ in 2021, this category experienced 736% growth from 2019, raising concerns that a small but increasing number of consumers are relying on BNPL for essential purchases as opposed to discretionary purchases.³⁸ In a qualitative discussion panel CR conducted in January 2023, some consumers indicated using BNPL for purchases to ease financial stress, including a single mom on unpaid sick leave using BNPL to get groceries for her family.³⁹

According to a CR survey, the percentage of Americans reporting ever having used a BNPL service was 21 in December 2022, or about 1 in 5. In terms of repeat usage, an August 2022 CR survey found that 16% of consumers indicated using BNPL once, 54% of users indicated using BNPL two to five times, 16% indicated using BNPL six to 10 times, 7% indicated using BNPL 11 to 20 times, and 8% indicated using BNPL more than 20 times, signaling that a segment of BNPL users are heavy repeat users.⁴⁰

³⁵ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

³⁶ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

³⁷ Total dollar volume of originations for lenders surveyed.

³⁸ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

³⁹ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

⁴⁰ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

In 2022, the average total sum of all of a user's BNPL purchases for the past year was \$2,085,⁴¹ while the average individual purchase amount financed by a BNPL loan was \$135 (in 2021).⁴²

Characteristics of BNPL users

The demographics of the user base for BNPL is not homogenous, perhaps reflecting the fact that the BNPL market is also not homogenous, with different providers targeting different consumer segments with different types of BNPL products. A mix of different income segments utilize BNPL, though usage is lowest for the highest income grouping (>\$200,000) and highest for those with household income between \$20,001 and \$50,000. Usage is lowest for those above age 65 and highest for those below age 35.⁴³

According to the CFPB, Black, Hispanic, and female consumers are significantly more likely to borrow using BNPL compared with white, non-Hispanic, and male consumers.⁴⁴ CR's August 2022 survey found that Black BNPL users are also more likely than other types of users to have used BNPL repeatedly; 40% of Black BNPL users have used BNPL at least six times, compared with 29% of Hispanic BNPL users and 27% of white BNPL users.⁴⁵

Of particular concern, substantial research shows that BNPL users are typically worse off financially than non-users. Compared with non-users, BNPL users: (1) are more likely to already have other credit products, (2) have lower savings and liquidity, (3) have lower credit scores, and (4) show more signs of financial distress.

BNPL users already have and use a number of credit products, suggesting that BNPL is frequently an additional credit product being utilized. A higher percent of BNPL users have open accounts in almost all credit products compared with non-BNPL users, with the exception of mortgages. For example, BNPL

⁴¹ Consumer Financial Protection Bureau, "Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey," March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

⁴² Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁴³ Consumer Financial Protection Bureau, "Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey," March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

⁴⁴ Consumer Financial Protection Bureau, "Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey," March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

⁴⁵ "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

borrowers are more likely than non-BNPL borrowers to use traditional credit products, including credit cards, retail cards, personal loans, auto loans, and student debt.⁴⁶

BNPL users also have lower savings and liquidity compared with non-BNPL users. BNPL users were found to have lower average non-retirement savings compared with non-users (\$3,887 vs. \$15,868) and 25% of BNPL users report having zero non-retirement savings or cash that could be used for emergencies (compared with 16% of non-BNPL users). Twice as many BNPL users as non-users (6% vs. 3%) have negative credit card liquidity, meaning their debt balances on all credit cards is higher than the sum of their credit card limits.

BNPL users have lower credit scores compared with non-BNPL users. TransUnion analysis in 2021 of 4 million BNPL users (as cited in a Harvard working paper) found that BNPL users have worse credit ratings compared with non-users, with 69% subprime or near prime.⁴⁷ Similarly, a 2022 TransUnion study found that subprime borrowers are significantly overrepresented among users of point-of-sale (POS) financing, representing 15% of the general population but making up 43% of POS users.⁴⁸

Lastly, BNPL users tend to show greater signs of financial distress compared with non-BNPL users. BNPL users utilize more high-cost loan products and exhibit greater delinquency. Compared with non-BNPL users, BNPL users had higher credit card utilization rates, higher incidence of revolving debt on credit cards, and higher utilization rates of high-cost alternative financial services such as payday loans, pawn shop loans, and overdrafts. Delinquency on any credit product was 18% for BNPL users compared with 7% for non-BNPL users.⁴⁹

BNPL users also exhibit greater signs of financial vulnerability. A Financial Health Network 2022 survey on BNPL found that financially vulnerable households⁵⁰ are nearly four times more likely to use BNPL than

⁴⁶ For example, 88% of BNPL users have an open credit card (compared with 75% of non-users), 32% have a personal loan (compared with 13%), 62% have an open retail card (compared with 44%), and 33% have a student loan (compared with 17%). See Consumer Financial Protection Bureau, “Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey,” March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

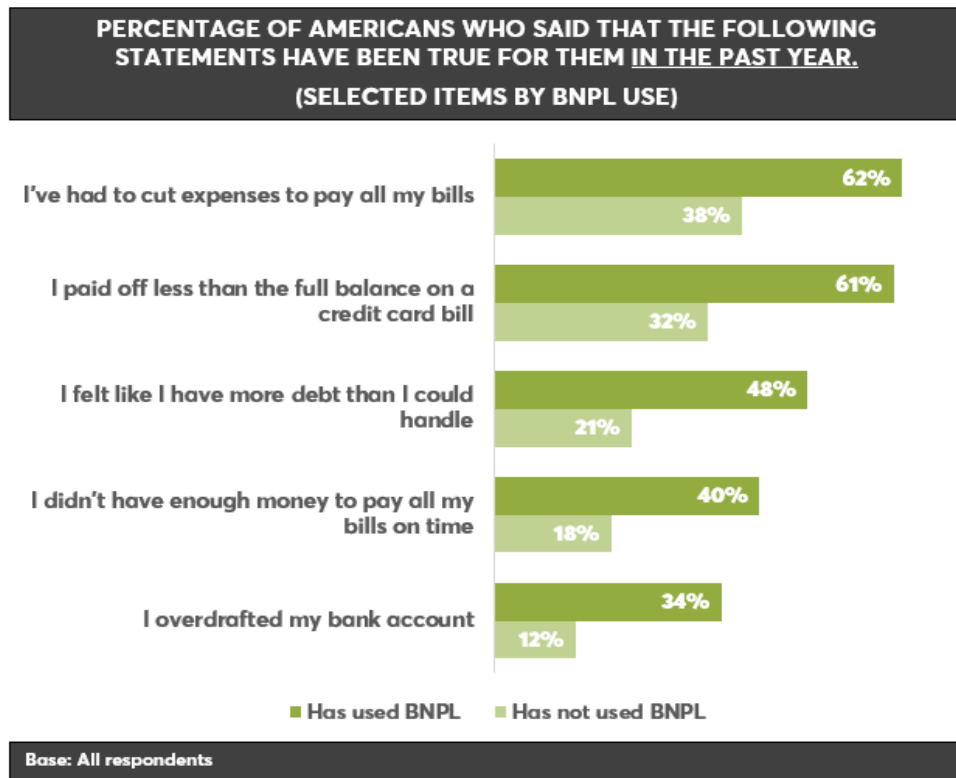
⁴⁷ TransUnion analysis as cited in Marshall Lux and Bryan Epps, “Grow Now, Regulate Later? Regulation urgently needed to support transparency and sustainable growth for Buy-Now, Pay-Later,” M-RCBG Associate Working Paper Series 2022.182, Harvard University, Cambridge, MA, April 2022, dash.harvard.edu/handle/1/37371375.

⁴⁸ “TransUnion Study Examines the Risk Profile of BNPL Applicants and the Financial Inclusion Opportunities that Exist for Both Consumers and Lenders,” *TransUnion*, May 25, 2022, newsroom.transunion.com/transunion-study-examines-the-risk-profile-of-bnpl-applicants--and-the-financial-inclusion-opportunities-that-exist-for-both-consumers-and-lenders.

⁴⁹ BNPL users had a credit card utilization rate (defined as credit card balance divided by the limit on all open, general purpose credit cards) of 40-50% compared with 30% for non-BNPL users. 69% of BNPL users were currently revolving on at least one credit card (meaning they carried over a credit card balance from one billing cycle to the next) compared with 42% of non-BNPL users. 42.8% of BNPL users used overdraft vs. 17.3% of non-BNPL users, 11.5% of BNPL users used payday loans vs. 2.9% of non-BNPL users, and 8.6% of BNPL users used pawn loans vs. 1.6% of non-BNPL users. See Consumer Financial Protection Bureau, “Consumer Use of Buy Now, Pay Later: Insights from the CFPB Making Ends Meet Survey,” March 2023, www.consumerfinance.gov/data-research/research-reports/consumer-use-of-buy-now-pay-later-insights-from-the-cfpb-making-ends-meet-survey.

⁵⁰ As measured using the Financial Health Network’s FinHealth Score®.

financially healthy households (18% vs. 5%), and 24% of BNPL users are financially vulnerable.⁵¹ A nationally representative CR survey in December 2022 found that compared with non-users, BNPL users were much more likely to have cut expenses to pay their bills and feel like they have more debt than they can handle.⁵² One participant in CR’s 2023 discussion panel noted that *“I would say if I was using a BNPL service, it’s because I’m already strained.”*⁵³



Consumer motivations for using BNPL

It is useful to better understand consumers’ motivations for using BNPL and their overall impressions of the product. In both cases, a mix of positive and negative responses highlights the need for nuanced policymaking in order to facilitate access to the positive aspects of BNPL products while addressing negative aspects.

BNPL providers often tout that BNPL provides consumers with convenience and the ability to better manage cash flow. Results from some demand-side surveys support these claims. One consumer survey found that the top reason for using BNPL was convenience (52.6%), followed by size of purchase (46.2%)

⁵¹ Hannah Gdalmán, Meghan Greene, and Necati Celik, “Buy Now, Pay Later: Implications for Financial Health,” Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

⁵² Consumer Reports nationally representative American Experiences Survey of 2,017 U.S. adults (December 2022), article.images.consumerreports.org/image/upload/v1672847923/prod/content/dam/surveys/Consumer_Reports_AES_December_2022.pdf.

⁵³ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

and ability to better manage finances (43.8%).⁵⁴ In CR's August 2022 survey, some consumers indicated using BNPL because they thought it would have lower interest rates and be easier to use than credit cards.⁵⁵

However, consumer surveys have surfaced other motivations that raise concerns. In both CR's and The Ascent's 2022 surveys, the top reason BNPL users cited for using BNPL was to make a purchase that the consumer could not afford to make otherwise, similar to credit cards.⁵⁶ These findings suggest that while some consumers are indeed utilizing BNPL products for convenience and lower cost, many consumers are utilizing BNPL to make purchases they could not otherwise afford, raising risks of overspending and overindebtedness, particularly for those BNPL users who are already overleveraged with traditional credit products.

Research on consumers' overall impressions of BNPL reflect a similarly mixed picture, again highlighting the fact that the user base for BNPL is not homogenous and the impacts (and potential harms) of BNPL will differ depending on the user segment. Overall, many consumers express a positive view of BNPL. In CR's discussion panel, consumers indicated that their favorite aspect of BNPL was the ability to easily spread out payments with no interest, particularly for those living paycheck-to-paycheck and needing to make bigger one-time purchases. Other consumers indicated being happy that they were able to buy something important to them that they could not afford otherwise, while some noted that BNPL filled a financial gap.⁵⁷ These results show that while some consumers are in a position to leverage and appreciate the income-smoothing aspect of BNPL, others are relying on the lending aspect of BNPL without fully appreciating its ramifications.

⁵⁴ Tom Akana, "Buy Now, Pay Later: Survey Evidence of Consumer Adoption and Attitudes," Federal Reserve Bank of Philadelphia, June 2022, www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/discussion-papers/dp22-02.pdf.

⁵⁵ "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf. "I thought it would have lower interest rates than a credit card," 11%; "I thought it would be easier than using a credit card," 11%.

⁵⁶ In CR's survey, the top reason for using BNPL cited by 45% of BNPL users was "I didn't have enough money to purchase what I wanted, so this enabled me to afford it." The second top reason was "I'd rather pay in installments instead of one lump sum," cited by 44% of BNPL users. See "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf. In The Ascent's survey, the top reason for using BNPL services cited by 45% of respondents was "to make purchases that otherwise wouldn't fit in my budget," followed by 37% of respondents citing "I want to avoid paying credit card interest." See "Study: Buy Now, Pay Later Services Grow in Popularity," The Ascent nationally representative survey of 2,000 U.S. buy now, pay later users (June 2022), www.fool.com/the-ascent/research/buy-now-pay-later-statistics.

⁵⁷ Consumer Reports, "Buy Now, Pay Later Online Discussion Panel," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

IV. Problematic Practices of BNPL Providers

As can be seen from the previous section, BNPL products can provide substantial value and benefit to some consumers. However, as with any financial product, BNPL products pose risks as well. These risks can arise from the credit aspect of the product, the way the products are marketed and sold, or the manner in which BNPL providers capture and use consumer data. A number of practices of BNPL providers that pose risks to consumers have been noted in the past. This section highlights the key practices of concern, including those that raise concerns due to the shift toward an app-based acquisition model, expansion to interest-bearing loans, and other market trends.

Wide variance and poor transparency in pricing structures

Poor disclosure and transparency practices for BNPL products have been long-standing concerns and remain so today. Many aspects of BNPL have caused confusion for consumers.

A fundamental issue is the sheer variety and inconsistency in pricing practices across the market. CR's research found that *"while most companies offer detailed explanations and terms of service, the nature, number, and complexity of different product options varies among companies."*⁵⁸ Some BNPL products include interest, while others do not. When users miss a repayment, some BNPL providers charge late fees, while others do not. Late fees may be imposed one day after the past due date or up to 10 days after, may be a fixed fee or a percentage of the loan amount, and may or may not be capped. Some BNPL providers charge a variety of other fees, such as reactivation fees. The current state of market practices inevitably leads to confusion among consumers who do not know what fees may be incurred under what conditions and at what point in time, which runs counter to consumer protection best practices.

For example, CR's research found the following types of fees and pricing practices across BNPL providers as of May 2023 (after reviewing fee disclosures, in-app notifications, and terms and conditions):⁵⁹

Affirm, PayPal	Do not charge late fees for their pay-in-four options but do charge an annual percentage rate (APR) for longer-term monthly options.
Afterpay, Klarna	Charge fixed late fees for their "interest-free" pay-in-four options, although these fees don't seem to make up a significant portion of their revenue.
Sezzle	Prevents users who fail to pay their installments on time from accessing their accounts and charges them a reactivation fee if they want to rejoin.

⁵⁸ Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁵⁹ Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

Zip	Charges both late fees and APRs.
Zilch	Says it charges zero fees on purchases made at its participating retailers but charges fees for any purchases online made with its Mastercard. Business model is unclear and potentially raises concerns about user privacy. ⁶⁰

Confusion caused by the wide range of pricing practices is likely exacerbated by the disconnect between the marketing of BNPL and the reality. As noted in CR’s report testing BNPL products, “*a primary issue of debate around BNPL loans is the veracity of the ‘no fee’ and ‘no interest’ claims made in marketing materials and alongside point-of-sale offers.*”⁶¹ BNPL products are heavily promoted as a “free” product, or even as a service (and not a loan). As a result, consumers may not realize that, contrary to marketing materials, they may incur varying costs associated with BNPL, including interest for longer term or larger BNPL loans and late fees in the case of late payments. In fact, CR’s August 2022 survey found that 3 out of 10 BNPL users said they were unaware of at least one of the possible fees or other penalties for late or missing payments at the time when they made their first BNPL purchase.⁶²

The format and timing of disclosed information is also critical to achieve clarity and transparency for consumers, and practices of BNPL providers are significantly lacking in this area. Information on fees and pricing practices is often scattered across various sources and buried in websites or in legal documents, rather than provided to consumers in a user-friendly, easily accessible manner and comprehensive format. In particular, “how terms and fee information are presented in-app implicates whether the true potential costs of the product are being clearly conveyed to consumers.”⁶³ In addition, one participant in CR’s discussion panel indicated that they were not notified that they would be charged interest for a BNPL loan until after their purchase had been completed.⁶⁴ Consumers should not be required to hunt down relevant information across multiple locations or channels, and should receive information early in the shopping process in order to make an informed decision about whether to use a BNPL product. As noted by one of CR’s discussion board participants:

⁶⁰ Zilch’s revenue model appears to be unique. Although the company seems to rely heavily on merchant fees, it has also created a proprietary advertising system called the Ad-Subsidized-Payments-Network that generates advertising revenue every time its customers make a purchase. Zilch then passes on a portion of this revenue to users “in the form of free credit, savings, deals, and discounts.” It’s unclear how this system works in practice and whether it poses any privacy concerns for users. See more at Zilch, “Googlisation of Payments: A \$1 Trillion Evolution of the Payments Model,”

www.zilch.com/news/googlisation-of-payments-a-1-trillion-evolution-of-the-payments-model.

⁶¹ Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁶² “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁶³ Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁶⁴ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

“It would have been nice if the exact details were more clearly stated as you go through the registration process because to me, it felt like they were keeping their cards close to their hand and not making it obvious to try and take advantage of someone not knowing exactly what they were getting into.”⁶⁵

Pricing information is currently not provided in a standardized manner, which further hampers consumer comprehension. Standardized cost-of-credit disclosures are typically required for credit cards and other types of consumer loans under the Truth in Lending Act (TILA), but such requirements have yet to be applied to traditional BNPL products. While some BNPL providers voluntarily provide TILA-like disclosures, not all providers follow this practice, resulting in inconsistency in the market and confusion and unexpected charges for consumers.

Multiple and excessive fees

BNPL providers also utilize problematic practices regarding the size of fees and the frequency with which they are charged.

As noted previously, BNPL late fee policies vary substantially. Some BNPL providers charge a flat fee, while others charge a percentage of the missed payment. For example, Afterpay states that it may charge up to a maximum of \$8 per missed payment,⁶⁶ while Zip charges from \$5 to \$10 per missed payment.⁶⁷ Several lenders reserve the right to charge multiple late fees for a single missed installment, which is an obviously problematic practice.⁶⁸ Affirm and PayPal do not charge any late fees.⁶⁹

⁶⁵ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

⁶⁶ Afterpay, “Installment Agreement,” www.afterpay.com/en-US/installment-agreement.

⁶⁷ Zip, “What happens if I don’t pay on time?” help.us.zip.co/hc/en-us/articles/360040937312--What-happens-if-I-don-t-pay-on-time.

⁶⁸ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁶⁹ Tom Akana, “Buy Now, Pay Later: Survey Evidence of Consumer Adoption and Attitudes,” Federal Reserve Bank of Philadelphia, June 2022, www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/discussion-papers/dp22-02.pdf. It appears that Klarna has also moved away from charging late fees, per the discussion in its 2021 annual report. See Klarna, “Annual Report 2021,” www.klarna.com/assets/sites/15/2022/03/28054307/Klarna-Bank-AB-Annual-report-2021-EN.pdf.

In 2021, 10.5% of BNPL users were charged at least one late fee, an increase from 7.8% in 2020.⁷⁰ Given the small size of the average BNPL loan (\$135 in 2021),⁷¹ late fees may add up to a significant cost for this segment of BNPL users, particularly if flat fees and/or multiple late fees are charged. For example, one participant in CR’s discussion panel indicated that they were charged a \$40 late fee on a \$70 purchase.⁷² While some BNPL lenders cap late fees based on the order amount or the amount of the missed payment, such as Afterpay (which caps fees at 25% of the order amount)⁷³ and Zip (which caps fees at a maximum of \$7 per late payment),⁷⁴ even these capped late fees may result in the equivalent of a high APR for an ostensibly “free” product.

In addition to late fees, some providers may also charge interest on the outstanding balance for missed or late payments. CR found that 28% of consumers with missed payments for BNPL loans said they were charged interest.⁷⁵

A wide range of other fees can also be incurred by BNPL users. For example, Sezzle charges fees when more than one payment for an order is rescheduled, reactivation fees when a payment has failed, and convenience fees when credit, debit, or prepaid benefit cards are used for a scheduled payment.⁷⁶

Consumers are also at risk of incurring overdraft fees or non-sufficient funds (NSF) fees from their other financial institutions if their repayments fail due to lack of funds. BNPL users are actually at risk of incurring multiple fees for failed payments, because BNPL lenders typically attempt to reauthorize failed payments, sometimes up to eight times for a single installment payment.⁷⁷ Given that the majority of BNPL repayments are set up on autopay, a failed payment is likely to mean that the consumer’s account

⁷⁰ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf. Other surveys have found a much higher incidence of BNPL users incurring late fees. For example, The Ascent’s June 2022 survey found that 33% of BNPL users have made a late payment or incurred a late fee. See “Study: Buy Now, Pay Later Services Grow in Popularity,” The Ascent nationally representative survey of 2,000 U.S. buy now, pay later users (June 2022), www.fool.com/the-ascent/research/buy-now-pay-later-statistics.

⁷¹ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁷² Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

⁷³ Afterpay, “Installment Agreement,” www.afterpay.com/en-US/installment-agreement.

⁷⁴ Zip, “Zip Customer Agreement,” zip.co/us/quadpay-terms-of-service. Note that the stated \$7 cap contradicts information found elsewhere on Zip’s website stating late fees of up to \$10.

⁷⁵ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁷⁶ Sezzle, “Why was I charged a fee?” shopper-help.sezzle.com/hc/en-us/articles/360046781511-Why-was-I-charged-a-fee.

⁷⁷ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

has insufficient funds, resulting in the user potentially incurring two sets of charges: late fees from the BNPL provider and overdraft or NSF fees from their financial institution.

The totality of the various fees described above and how they are applied are a concern that goes beyond clear disclosure. Cumulatively, such fees may add up to significant costs for a small loan. If such fees are not linked to actual provider costs related to the BNPL product and are being used to generate revenue, these fee practices raise questions regarding fairness.

Automatic repayments and use of credit cards for repayment

As noted previously, BNPL providers typically require users to set up automatic repayments via debit or credit cards as a default when first obtaining a BNPL loan. CR's research found that 69% of users' BNPL purchases involve automatic repayments (as opposed to manual repayments).⁷⁸

While automatic repayment provides certain benefits to consumers by ensuring that consumers won't miss a repayment by accident, there are risks involved as well. One problem arises from the fact that some BNPL providers make it difficult or impossible to remove autopay. Again, providers' policies and practices were found to differ substantially. One lender allows borrowers to change repayment methods via a self-service online portal, another allows borrowers to do so by contacting customer service, and two BNPL lenders do not allow borrowers to turn off autopay.⁷⁹

Mandating autopay goes against good practice, because consumers should have choice and control over any withdrawals from their accounts, for example if they are in a situation where it is necessary to prioritize certain repayments over others. When linked to bank accounts, automatic repayment brings the added risk of potentially triggering overdraft fees or non-sufficient funds, resulting in the consumer incurring significant (relative to BNPL loan sizes) and unexpected costs.

The use of credit cards for repayment of BNPL loans is inherently problematic, because it conflicts with the concept of an "interest-free" BNPL loan. BNPL users are at risk of incurring more debt (if they have revolving credit card debt) and debt with potentially high interest. CFPB research found that credit cards were used to make 10.1% of BNPL installment payments in 2021,⁸⁰ while CR's research found that 24% of BNPL users indicated using a credit card for BNPL repayments.⁸¹

⁷⁸ "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁷⁹ Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁸⁰ Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁸¹ "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

Limited assessment of repayment capacity

BNPL providers do not conduct the typical assessment of an applicant's ability to repay, particularly for "traditional" pay-in-four BNPL products. Instead, many employ a "low and grow" strategy, extending limited amounts to first-time borrowers and gradually increasing the amount extended as borrowers exhibit positive repayment behavior. For new customers, BNPL providers will often only verify the customer's identity, require a debit card or credit card to make payment, and run a "soft" credit check. Some BNPL providers consider credit scores as part of their general underwriting process. But most BNPL providers do not conduct a full assessment of a consumer's ability to repay the BNPL loan, including considering other debt obligations against a consumer's income and assets and determining whether there is sufficient income to repay the loan.⁸² Even if BNPL providers were to conduct a full assessment of a prospective user, comprehensive data on BNPL loans is lacking in credit bureaus (a topic that will be discussed below). As a result, some consumers may be receiving BNPL loans that they are incapable of repaying (at least without suffering hardship).

Inconsistent credit reporting

Current practices in the BNPL market pose a range of risks regarding consumer's credit scores. To begin with, BNPL providers do not consistently report to consumer reporting agencies (CRAs), though this practice appears to be changing to some degree. As a result, there is a lack of visibility in CRAs with respect to a consumer's BNPL activity with other providers, which could lead to a consumer having multiple concurrent BNPL loans with different lenders at the same time.

Approaches appear to be quite inconsistent across the market, with some BNPL providers not reporting any BNPL loans to CRAs, some reporting payment history to all CRAs, some reporting only some loans to a single CRA, and others reporting only positive payments for certain BNPL products. CR's review of BNPL companies' publicly available documentation in 2023 found that Afterpay, PayPal, Sezzle, and Zip do not report BNPL loans to CRAs. Perpay reports payment history to all three CRAs, while Affirm reports some loans only to Experian. Lastly, Zilch reports positive payments to credit bureaus, but not for zero percent loans with four biweekly payments or a three-month repayment period.⁸³

⁸² Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁸³ It is worth noting that the reporting practices described here differ substantially from those described in a 2022 report from the Federal Reserve Bank of Philadelphia (FRBP), which was also based on review of online terms and conditions. The FRBP report found that Affirm and Afterpay do not report late or non-payments on pay-in-four products to CRAs, PayPal will report missed payments, and Klarna and Zip may report missed payments or defaults. These marked differences suggest that BNPL companies' credit reporting policies are rapidly evolving and currently in flux. See Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf. See also Tom Akana, "Buy Now, Pay Later: Survey Evidence of Consumer Adoption and Attitudes," Federal Reserve Bank of Philadelphia, June 2022, www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/discussion-papers/dp22-02.pdf.

The current situation creates confusion and uncertainty for consumers. Without consistent reporting, consumers cannot benefit from the (potential) upside of positive repayment behavior. But it appears that consumers may already be experiencing the downside of reporting on late or missed payments. In a 2022 CR survey, 15% of consumers who missed one or more BNPL payments stated that the debt appeared on their credit report.⁸⁴

An additional concern is that simply using BNPL could harm consumers' credit scores, even when repaid on time. If BNPL loans are treated as a series of small-dollar installment loans that are opened and closed over a short time period, the inclusion of BNPL loans will actually negatively impact consumer's credit scores due to FICO algorithms that factor in length of credit history and new credit.⁸⁵

Part of the current confusion stems from the fact that CRAs have yet to develop a consistent and appropriate approach on how to treat BNPL data given its unique characteristics, a concern flagged by the CFPB.⁸⁶ The three major CRAs have all begun collecting BNPL data but are keeping that data separate from core credit bureau data for now. This is as a short-term solution to ensure that BNPL data will not negatively impact consumers' credit scores.⁸⁷

Exploitation of behavioral biases

The practices of BNPL providers raise concerns regarding the exploitation of consumers' behavioral biases, particularly given the shift to app-driven acquisition models. These practices (and the related concerns for consumers) are not limited to the BNPL industry, but have arisen with respect to digital ecosystems more broadly. The very manner in which BNPL is pitched to merchants centers around BNPL's ability to "convert" customers and increase the amounts that customers spend. Digital platforms such as

⁸⁴ "Buy Now, Pay Later Services," Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁸⁵ For further details, see Center for Responsible Lending, National Consumer Law Center, and Consumer Federation of America. "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, March 25, 2022, www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-nclc-cfa-comment-buynow-paylater-mar2022.pdf.

⁸⁶ Consumer Financial Protection Bureau, "Buy Now, Pay Later and Credit Reporting," June 2022, www.consumerfinance.gov/about-us/blog/by-now-pay-later-and-credit-reporting.

⁸⁷ Equifax, "Equifax First to Formalize Inclusion of 'But Now, Pay Later' Payment Information in Consumer Credit Reports," press release, December 20, 2021, investor.equifax.com/news-events/press-releases/detail/1204/equifax-first-to-formalize-inclusion-of-buy-now-pay. Business Wire, "Experian's Industry-first Buy Now, Pay Later Bureau Will Protect Consumer Credit Scores and Provide Real-time Insights to Drive More Inclusive and Responsible Lending," January 2022, www.businesswire.com/news/home/20220127005299/en/Experian%E2%80%99s-Industry-first-Buy-Now-Pay-Later-Bureau-Will-Protect-Consumer-Credit-Scores-and-Provide-Real-time-Insights-to-Drive-More-Inclusive-and-Responsible-Lending. TransUnion, "TransUnion to Maximize Financial Inclusion Opportunities for the Nearly 100 Million Consumers Using BNPL Loans," February 2022, newsroom.transunion.com/transunion-to-maximize-financial-inclusion-opportunities-for-the-nearly-100-million-consumers-using-bnpl-loans.

BNPL platforms are being designed using deceptive designs⁸⁸ in order to affect users' self-control and lead them toward certain choices, namely to spend more and more frequently.

A 2021 study found instances of deceptive designs in two leading Swedish BNPL lenders, one of which has a significant presence in the U.S. Ten different deceptive designs were found to be employed, including:⁸⁹

- One instance based on color, defined as “overshadowing the non-target action by using a higher contrast color scheme for the target action.”
- Four instances were based on “false hierarchy,” defined as “interactive precedence over the non-target actions, in instances where the target action is visualized hierarchical rather than parallel.”
- One instance was based on “hidden information,” defined as “hiding the non-target action, making it not immediately or readily accessible.”
- Two instances were based on “preselection,” defined as “the target action being selected by default previous to user interaction.”
- Two instances were based on “nagging,” defined as “the minor redirection of an expected outcome, and is often repeated intrusion where the designers are steering the user away from non-target actions, into their own target actions through nagging.”

Use of deceptive designs and exploitation of behavioral biases can lead consumers to take out more credit than they otherwise would, overestimate their ability to repay, and underestimate the consequences, ultimately leading to harm to their financial well-being.

Data harvesting and data privacy

The practice of data harvesting is closely linked to exploitation of behavioral biases and is similarly a broader, growing issue found across the digital ecosystem. As mentioned in Section II, current trends in the BNPL market, particularly the shift to an app-based acquisition model, has also shifted the opportunities and incentives for BNPL providers. As a full-service shopping experience with an ongoing relationship with customers, BNPL platforms will have access to substantial amounts of proprietary data on customers' shopping and spending patterns. This data can be used to inform the design of user interfaces (UI) and user experience (UX) in order to push consumers toward desired actions.

Customer data can also be harvested and monetized. BNPL providers can utilize data to develop digital profiles of users' shopping preferences and behaviors, which can then be leveraged to provide data-driven services to merchants, such as targeted ads and personalized content, promotions, and offerings. As noted by the CFPB, data mining a consumer's behavioral surplus⁹⁰ may ultimately offer “the

⁸⁸ The terms “deceptive designs,” “deceptive design patterns,” “deceptive patterns,” and “dark patterns” have been used interchangeably to describe design practices that trick or manipulate users into making choices they would not otherwise have made and that may cause harm. For purposes of this report, the term “deceptive designs” is being used to refer to these practices. See Federal Trade Commission, Staff Report, “Bringing Dark Patterns to Light,” September 2022, www.ftc.gov/reports/bringing-dark-patterns-light.

⁸⁹ Isabella Johannesson, “Dark Patterns in Digital Buy Now Pay Later Services,” KTH Royal Institute of Technology, 2021, kth.diva-portal.org/smash/get/diva2:1588606/FULLTEXT01.pdf.

⁹⁰ “Behavioral surplus” refers to pieces of consumer-provided or consumer-derived data that add value to models that predict the brands and products that are most likely to elicit clicks and purchases. The term was first

highest long-term value to BNPL lenders”⁹¹ of any revenue source, particularly as BNPL providers seek to achieve a sustainable business model. BNPL providers have already begun promoting such services to prospective merchant clients.⁹²

As with many innovations in the digital economy, these practices can have both benefits and risks to consumers. While some consumers may benefit from targeted ads and promotions, such practices are designed to drive repeat usage and higher spending levels, leading to the risk of overspending by consumers and harm to consumer welfare. The line between what is acceptable marketing vs. unfair exploitation of consumers remains unclear.

More broadly, such practices raise questions regarding data privacy and user control. In the digital ecosystem, consumers continue to face many challenges in controlling the collection and use of their personal data, let alone the data generated by their use of digital products and services. Many consumers have already expressed concerns regarding BNPL providers sharing their data. A 2022 CR survey found that 24% of respondents were very concerned about BNPL providers sharing their personal data, for example with companies that want to market products to them, while another 44% of respondents were somewhat concerned.⁹³

These concerns prove to be well founded. CR’s testing of BNPL products found that all BNPL apps tested used ambiguous and open-ended language in privacy policies, such as stating that personal information will be used for “legitimate business purposes,” which can be interpreted quite broadly.⁹⁴ Some BNPL providers disclose data collection, usage, and sharing practices that go beyond what is strictly necessary for the core function of the BNPL service being provided, such as collecting data on internet browsing history and email and chat communications⁹⁵ and using personal information for marketing or targeted advertising.

The vast majority of BNPL providers’ policies state that they can share data with third parties. CR’s product testing of BNPL apps found that *“though companies may not sell data, data can be exchanged for ‘other forms of value’ (Klarna), used in consumer profiles from which analytics may be shared with*

popularized by Shoshana Zuboff’s book “The Age of Surveillance Capitalism: The Fight for a Human Future at the New Frontier of Power” (PublicAffairs, 2019).

⁹¹ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

⁹² For example, Klarna highlights its capabilities for segmented targeting of customers for ads and sponsored content (see www.klarna.com/us/business/marketing-solutions/ads-sponsored-content/), while Zip highlighted the ability to deliver targeted messages, promotions, and merchant content in its 2021 annual report (see zip.co/investors/app/uploads/2021/05/annual-report-2021.pdf).

⁹³ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

⁹⁴ Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁹⁵ Some BNPL apps request users to grant permission for the collection of these types of additional data.

*third parties (Affirm), transferred outright, or shared with third parties.*⁹⁶ As a result, consumer data can be shared or transferred to affiliated or non-affiliated third parties for marketing or targeted advertising purposes.

An additional challenge for consumers is poor, confusing, and at times contradictory disclosure of data-sharing practices. For example, CR's testing of BNPL apps found that *"the range of practices and variations in the way these practices are described are so diverse, complex, and, at times, vague, that it is difficult to impossible for any user to determine what is actually happening with their data."*⁹⁷ In fact, numerous instances were encountered of companies explicitly stating that they do not sell or share consumer data for marketing purposes, but review of disclosures in privacy policies found contradictory language specifying the very type of data sharing that companies said they did not engage in.

In some cases, consumers are provided with controls over certain privacy settings, though these can be difficult to utilize in practice. Only one BNPL app tested was found to provide comprehensive privacy controls to users. Some BNPL apps had limited privacy settings that users could control for certain aspects, such as turning off personalized ads or opting out from being remembered by merchants. Other BNPL apps provided no privacy controls at all that users could adjust, or no easy means to find such controls. Notably, CR's testing found that *"some companies considered in-app shopping and marketing features as core to the business, thus they do not offer the functionality to turn off targeted advertising within the app."*⁹⁸ At the same time, apps may default to settings that are less beneficial to consumers. For example, most BNPL companies opt consumers into third-party data sharing by default. Consumers must then actively locate privacy settings (if available) and opt out of data sharing in order to stop this practice.⁹⁹

Challenges with returns

A final BNPL practice that has raised long-standing issues for consumers is the treatment of returns. In 2021, 13.7% of individual BNPL loans had at least some portion of the order returned.¹⁰⁰ Unfortunately,

⁹⁶ Seven out of 8 BNPL providers tested indicated sending data to companies involved in advertising or e-commerce. Only 1 out of 8 companies tested commits to not sell or share data with non-affiliates for advertising purposes. Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁹⁷ Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁹⁸ Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

⁹⁹ Seven out of 8 BNPL providers tested indicated sending data to companies involved in advertising or e-commerce. Only 1 out of 8 companies tested commits to not sell or share data with non-affiliates for advertising purposes. Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

¹⁰⁰ Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

CR’s discussion panel found that several consumers who tried to make a return faced difficulties when doing so, particularly with the time and complexity involved in the return process.¹⁰¹

BNPL policies toward returns are both unclear and inconsistent. To begin with, it is not clear whether to initiate returns with the BNPL provider or the merchant. Some BNPL providers require consumers to first contact merchants to initiate returns. If a merchant declines to authorize a refund for a disputed item, then consumers can contact the BNPL provider to file a dispute, after which the BNPL will begin an investigation. Given the multiple parties involved in disputes and the back-and-forth nature of communications, the dispute process may end up being lengthy and complicated for consumers. Consumers have even described instances in which a BNPL lender and a merchant were “pointing fingers at each other” and the consumer was “left holding the bag.”¹⁰²

The lack of clear and consistent dispute resolution processes not only poses frustrating logistical challenges to consumers but also can cause financial harm. Consumers are often required to continue making installment payments while disputes are being investigated, in some cases even after a product has been returned. Practices toward requiring repayments in the midst of a dispute vary by BNPL provider. One BNPL provider was found to require continued payments pending a dispute, two lenders allow the borrower to defer payment for a short time following a reported dispute, and two lenders stop payment indefinitely during a reported dispute.¹⁰³

¹⁰¹ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

¹⁰² Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

¹⁰³ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

V. Broader Potential Harms to Consumers

As shown in Section IV, problematic practices of BNPL providers can lead to a variety of discrete harms to consumers. For some consumers, BNPL practices also have the potential to lead to two broader harms: overindebtedness and overspending.

Overindebtedness

The cumulative effect of the problematic practices discussed in Section IV—including poor disclosure of pricing and fees, limited assessment of the capacity to repay, inconsistent reporting to CRAs, and exploitation of behavioral biases—can result in consumers becoming overindebted. As noted in a 2022 paper on BNPL from the Harvard Kennedy School:

“For consumers with high financial literacy, strong credit scores, and easy access to credit, BNPL can offer substantial improvements in the timing of payments and inconvenience at POS. For consumers who already struggle to manage their personal finances, though, BNPL can facilitate spending beyond capacity to pay.”¹⁰⁴

Existing data shows that some consumers are taking on multiple BNPL loans and missing payments, which may signal increasing overindebtedness. Given the ease of obtaining a BNPL loan, the lack of a full assessment of capacity to repay, and inconsistent credit reporting, consumers may end up taking out multiple BNPL loans concurrently, raising the risk of overextension. CR’s August 2022 survey showed that 17% of BNPL users had two concurrent BNPL installments, 7% had three, 7% had four, 1% had five, and 2% had six or more.¹⁰⁵ One participant in CR’s discussion panel was not even aware that she had three BNPL loans open (at one BNPL provider) until she checked her account as part of the research exercise.¹⁰⁶

A not insignificant portion of BNPL users have missed payments on BNPL loans. One source found that 14% of BNPL users have missed one payment, while 12% have missed more than one payment.¹⁰⁷ Financially vulnerable consumers and consumers with concurrent BNPL loans are much more likely to have missed payments. The Financial Health Network found that financially vulnerable users were three

¹⁰⁴ Marshall Lux and Bryan Epps, “Grow Now, Regulate Later? Regulation urgently needed to support transparency and sustainable growth for Buy-Now, Pay-Later,” M-RCBG Associate Working Paper Series 2022.182, Harvard University, Cambridge, MA, April 2022, dash.harvard.edu/handle/1/37371375.

¹⁰⁵ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

¹⁰⁶ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

¹⁰⁷ Piplsay survey of 31,000 U.S. consumers from September 2020-September 2021. Cited in Julian Alcazar and Terri Bradford, “The Appeal and Proliferation of Buy Now, Pay Later: Consumer and Merchant Perspectives,” Federal Reserve Bank of Kansas City, November 2021, www.kansascityfed.org/research/payments-system-research-briefings/the-appeal-and-proliferation-of-buy-now-pay-later-consumer-and-merchant-perspectives.

times as likely as overall users to report difficulty in making payments,¹⁰⁸ while CR's August 2022 survey found that BNPL users with four or more concurrent BNPL loans were twice as likely to have missed a payment compared with those with fewer concurrent BNPL loans.¹⁰⁹

As discussed in Section II, compared with non-BNPL users, BNPL users are more likely to have a range of existing credit products and lower savings and liquidity, and to show signs of financial distress (such as utilizing high-cost loan products and exhibiting greater delinquency). As a result of these pre-existing debt loads and financial constraints, BNPL users are therefore more vulnerable to harm to their financial health due to overuse of BNPL. For example, research has found that “new BNPL users experience rapid increases in bank overdraft charges and credit card interest and fees, as compared to non-users,” which is consistent with declines in leading indicators of financial health.¹¹⁰

Sustained usage of BNPL may also harm consumers' ability to meet other obligations and trap consumers in debt cycles. As noted by the CFPB, “frequent BNPL usage may threaten borrowers' ability to meet non-BNPL financial obligations, such as rent, utilities, mortgages, auto loans, and student loans.”¹¹¹ Research by the Australian Securities & Investments Commission (ASIC) found that 20% of BNPL users cut back or went without essential items in order to make payments, while 15% of people took out other loans to make a BNPL payment.¹¹² In the U.S., one survey found that 32% of respondents had to “delay or skip paying an essential bill due to the payments on [their] Buy Now Pay Later plans.”¹¹³

Overspending

While overindebtedness arguably has the potential to cause greater harm to a segment of BNPL users, overspending is also detrimental to consumer welfare and is likely to impact a greater proportion of BNPL users than overindebtedness. BNPL is engineered to exploit temptation bias and encourage impulse buying, leading consumers to spend more and more frequently. Data shows that it is quite successful in this regard.

Similar to credit cards, BNPL appears to have a direct impact on how much consumers end up spending on a purchase. In fact, this characteristic is consistently touted by BNPL providers in materials aimed at

¹⁰⁸ Hannah Gdalmán, Meghan Greene, and Necati Celik, “Buy Now, Pay Later: Implications for Financial Health,” Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

¹⁰⁹ “Buy Now, Pay Later Services,” Consumer Reports nationally representative internet survey of 2,013 U.S. buy now, pay later users (August 2022), advocacy.consumerreports.org/wp-content/uploads/2022/11/2022-Consumer-Reports-Buy-Now-Pay-Later-Survey-Report.pdf.

¹¹⁰ Ed deHaan, Jungbae Kim, Ben Lourie, and Chenqi Zhu, “Buy Now Pay (Pain?) Later,” SSRN, September 27, 2022, papers.ssrn.com/sol3/papers.cfm?abstract_id=4230633.

¹¹¹ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

¹¹² Australian Securities & Investments Commission, “Buy now pay later: An industry update,” Report 672, November 2020, download.asic.gov.au/media/5852803/rep672-published-16-november-2020-2.pdf.

¹¹³ “Survey: Buy Now Pay Later Plans Fuel Debt Struggles,” DebtHammer nationally representative survey of 1,050 U.S. buy now, pay later plan users (February 2022), debthammer.org/buy-now-pay-later-survey.

merchants and investors. Klarna claims that consumers typically spend 68% more when using BNPL.¹¹⁴ Affirm similarly notes that its merchant clients experience an 85% increase in Average Order Value (AOV) when consumers opt to use its BNPL plan over other payment methods.¹¹⁵ Academic research has found that access to BNPL even leads to increases in a consumer's total spending, beyond simply the item purchased using BNPL.¹¹⁶ Unsurprisingly, the same paper also noted that BNPL use results in increased likelihood of accessing savings and incurring overdraft, NSF, and other late fees.

BNPL also leads to repeat usage. One BNPL lender reports that 65% of BNPL is from repeat users, while another reports an 80% increase in repeat customer rate.¹¹⁷

The inclination to spend more with BNPL leads many consumers to make purchases that they would otherwise not have made. A 2022 Financial Health Survey found that 30% of BNPL users reported having spent more than they would have if BNPL was not available. In addition, 34% of BNPL users said they would not have made the purchase at all if the BNPL option had not been available.¹¹⁸ Numerous surveys indicate that between 20% and 50% of BNPL users regret their purchases afterward.¹¹⁹

Given that many BNPL users are already financially strained, these incidences of overspending are concerning and likely to cause real harm to consumers' overall financial well-being, even if they are not tipped into a state of overindebtedness.

¹¹⁴ Klarna, "Deep Dive," www.klarna.com/assets/sites/2/2020/01/21085652/klarna-deep-dive.pdf.

¹¹⁵ Affirm, Fiscal Q4 2021 "Investor Presentation," Fiscal Q4 2021, investors.affirm.com/static-files/18f24d87-9ccd-4e3d-9253-dff937441677.

¹¹⁶ The report found that BNPL use causes a permanent increase in total spending of around \$60 per week, primarily concentrated in retail spending. See Marco Di Maggio, Emily Williams, and Justin Katz, "Buy Now, Pay Later Credit: User Characteristics and Effects on Spending Patterns," National Bureau of Economic Research, Working Paper 30508, September 2022, www.nber.org/papers/w30508.

¹¹⁷ Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

¹¹⁸ Hannah Gdalmann, Meghan Greene, and Necati Celik, "Buy Now, Pay Later: Implications for Financial Health," Financial Health Network, March 2022, finhealthnetwork.org/wp-content/uploads/2022/03/Buy-Now-Pay-Later-Brief-2022.pdf.

¹¹⁹ Consumer Financial Protection Bureau, "Buy Now, Pay Later: Market Trends and Consumer Impacts," September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

VI. Policy Measures to Mitigate BNPL Risks to Consumers

A wide range of measures can be utilized to address the various risks that BNPL poses to consumers. The suggestions included below are not intended to be exhaustive, nor meant to be implemented all at once, but rather to serve as a menu that can be drawn from by both policymakers and market players.

Enhanced disclosure and transparency

At a minimum, BNPL providers should be required to make clearer distinctions between “traditional” pay-in-four, interest-free products and other types of BNPL products that are longer term and interest-bearing. The differences between these products should be clearly conveyed during both the shopping stage (in marketing materials and on websites, apps, etc.) as well as during the transaction stage. Where a BNPL product comes with interest, this fact should be conveyed to a consumer early in the transaction process and preferably require confirmation from the consumer before proceeding in the transaction, in order to ensure consumer comprehension. For BNPL products that come with interest or are split between more than four installment payments, Truth in Lending Act requirements should be complied with.

For “traditional” BNPL products, a set of disclosure requirements should be developed that is tailored to the characteristics of BNPL products and ensures that key information is conveyed to consumers in a more standardized and user-friendly format. Information to be disclosed should include key product terms and features, including payment due dates, late fees, and how and when fees are applied, as well as dispute resolution processes. Given that late fees are incurred by a fair number of BNPL users and represent a significant cost relative to the size of BNPL loans, BNPL providers could be required to present an APR equivalent that includes late fees so that consumers are made clearly aware of the potential cost of this ostensibly “free” product and can easily compare this potential cost with other loan products, such as credit cards.

BNPL providers should also be required to disclose the risks associated with BNPL products and provide warnings to consumers. This should include upfront, clear warnings regarding late fees,¹²⁰ but also the potential for users to incur overdraft fees, NSF fees, or interest on credit cards if credit cards are being used for repayment. Potential impacts of BNPL products on consumers’ credit scores should also be clearly conveyed.

BNPL providers should be encouraged to integrate an intermediate step in the digital transaction process, which can serve dual purposes. A purchasing process that is too quick has been shown to be detrimental to consumer decision-making.¹²¹ Requiring consumers to pause and reflect during a digital transaction process may therefore help lead consumers to make more optimal choices. In addition, given that some consumers are not fully aware that BNPL is a loan, an intermediate step can also be used to convey a reminder to consumers that they are taking out a loan product and that they should be sure that they have sufficient funds to repay the BNPL loan within the next six weeks.

¹²⁰ Policymakers could also consider requiring BNPL companies to disclose the average frequency with which the respective company’s users incur late fees.

¹²¹ European Commission, Consumers, Health, Agriculture and Food Executive Agency, “Behavioral Study on the Digitalisation of the Marketing and Distance Selling of Retail Financial Services — Executive Summary: April 2019,” Publications Office, 2019, data.europa.eu/doi/10.2818/644670.

Behaviorally driven design and the digital medium can and should be leveraged to enhance transparency, particularly given that most BNPL transactions occur online. CR’s product testing found that despite the mobile app environment, BNPL apps consistently relied on long-form disclosures not well suited for digital channels, and in particular mobile channels.¹²² At a minimum, disclosed information should be adapted to be user-friendly to review via digital channels. Any standardized formats for disclosure should ideally incorporate behavioral design techniques to improve consumer engagement and comprehension and be tested with consumers before being utilized. User interfaces should be designed to be easily navigable by consumers, with pop-ups, layering of information, push notifications, and icons or symbols (ideally standardized across the industry) employed to convey information in a more user-friendly manner via digital channels.¹²³

Lastly, BNPL providers should be encouraged to provide user-friendly digital tools to aid consumers in tracking outstanding BNPL loans, due dates, and repayment amounts, given that some BNPL users have multiple concurrent loans and consumers have indicated that it can be difficult to keep track of many small loans and payment dates.¹²⁴

Responsible lending

BNPL providers should generally be required to assess a consumer’s ability to repay in order to mitigate the risk of overextension. Requirements applicable for credit cards under the Truth in Lending Act could be extended to cover BNPL loans.

However, policymakers may wish to consider an exception for the smallest “traditional” BNPL loans, in order to accommodate BNPL providers that utilize a blind, “lend-to-learn” model for new users. As an alternative, tailored requirements could be developed for such models that still seek to ensure responsible lending via other means. For example, the exception could be limited to loans below a certain size (such as \$500). BNPL providers seeking to utilize alternative scoring methods to traditional assessments of repayment capacity could be required to monitor performance on an enhanced basis and take action in the case of an increase in missed payments. Restrictions could be placed on lending to consumers who have missed multiple payments. Some BNPL providers already say they restrict use of services if a payment is missed in order to prevent debt from accumulating.

In addition to requiring assessments of the ability to repay, other responsible lending measures could be considered. For example, the number of concurrent BNPL loans a borrower can have outstanding could be capped (such as a cap of five concurrent loans). Some BNPL providers already utilize such a practice,

¹²² Consumer Reports, “Buy Now, Pay Later: A Case Study for a Digital Finance Standard,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

¹²³ For example, experimental research has shown that disclosure boxes and disclosure pop-ups can increase consumer comprehension regarding BNPL. See Paul Adams, “Buy Now Pay Later: An experimental approach to improving comprehension and decision making,” CogCo, December 2022, www.citizensadvice.org.uk/Global/CitizensAdvice/Consumer%20publications/Buy%20Now%20Pay%20Later%20Experimental%20Research%20Public%20Report.pdf.

¹²⁴ Consumer Reports, “Buy Now, Pay Later Online Discussion Panel,” May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/BNPL-Discussion-Board-Jan2023-Report.pdf.

though this is not currently standard in the industry.¹²⁵ Under the app-based acquisition model, consumers are pre-approved for what essentially acts like a short-term line of credit. BNPL providers could be required to limit how long this quasi line of credit remains available (for example, to one month) and be prohibited from increasing the quasi line of credit except at the user’s request.

Credit reporting

BNPL providers should be required to report both positive and negative repayment information to CRAs. In parallel, policymakers should work with the industry to develop an appropriate, standardized approach for how to treat BNPL data. For example, stakeholders could explore utilizing the approach of treating BNPL loans as an open-ended line of credit as opposed to a series of short-term, closed-end loans. The pros and cons of various approaches will need to be examined in greater depth in order to develop an appropriately balanced approach.

Fair marketing

Policymakers should take steps to ensure that marketing for BNPL products is not misleading. For example, where a BNPL provider offers multiple BNPL loans with interest, or where most customers incur fees when using the product, marketing should not focus solely on promoting the “free” nature of BNPL products.

With respect to the use of deceptive designs, a topic that extends beyond BNPL and is broader than this report can address, two measures could be considered, one practical and the other more ambitious and forward-looking. In the past, the Federal Trade Commission (FTC) has highlighted categories and examples of deceptive designs¹²⁶ and indicated that the use of deceptive designs may be in violation of the FTC Act, as well as other statutes and regulations. The FTC has also sued some companies for utilizing certain deceptive designs and issued an enforcement policy statement warning companies against

¹²⁵ Consumer Financial Protection Bureau, “Buy Now, Pay Later: Market Trends and Consumer Impacts,” September 2022, files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

¹²⁶ The categories include the following: (1) Endorsements (aka “social proof”)—e.g., false activity messages, deceptive consumer testimonials, deceptive celebrity endorsements, parasocial relationship pressure; (2) Scarcity—e.g., false stock message, false high demand message; (3) Urgency—e.g., baseless countdown timer, false limited time message, false discount claims; (4) Obstruction—e.g., price comparison prevention, roadblocks to cancellation, immortal accounts; (5) Sneaking or information hiding—e.g., sneak-into-basket, hidden information, hidden costs, drip pricing, hidden subscription or forced continuity, intermediate currency; (6) Interface interference—e.g., misdirection, false hierarchy or pressured upselling, disguised ads, bait and switch; (7) Coerced action—e.g., unauthorized transactions, auto-play, nagging, forced registration or enrollment, pay-to-play or grinding, friend spam/social pyramid schemes/address book leeching; and (8) Asymmetric choice—e.g., trick questions, confirm shaming, pre-selection, subverting privacy preferences. See Federal Trade Commission, Staff Report, “Bringing Dark Patterns to Light,” September 2022, www.ftc.gov/reports/bringing-dark-patterns-light.

deploying certain deceptive designs.^{127, 128} At a practical level, it may be useful to examine what specific deceptive designs are being utilized by BNPL providers in the U.S. and provide more explicit guidance to the BNPL industry on which types of deceptive designs are considered in clear violation of existing laws and regulation. Without strong guardrails in place for the entire market, a responsible company that refrains from using deceptive designs could be placed in a disadvantageous position vs. competitors that continue to employ deceptive designs.

On a more forward-looking basis, policymakers could explore developing a principles-based “fairness by design” approach and encouraging responsible digital architecture. As opposed to, or in addition to, providing clear prohibitions on deceptive designs, providers could be given greater responsibility or duty to develop digital architecture that is designed to be fair for consumers. Such an approach would be similar to growing efforts to introduce “privacy by design” and product design requirements to protect consumers on an ex ante basis by requiring providers to consider consumer well-being in the design phase. For example, the United Kingdom government has indicated that it is considering how to champion “fairness by design” principles for online transactions,¹²⁹ while the Australian Competition & Consumer Commission (ACCC) is considering a broad, principles-based obligation requiring platforms to present information and choices in a way that is accessible, balanced, and empowers consumers to exercise their settings and controls.¹³⁰

Stronger data privacy

As with deceptive designs, data harvesting and data privacy are topics that extend beyond BNPL. However, it is worth reiterating here that there is an urgent need for stronger data privacy standards in the U.S., including in the financial sector. In CR’s Fair Digital Finance testings, which to date include

¹²⁷ Federal Trade Commission, “Enforcement Policy Statement Regarding Negative Option Marketing,” November 2021, www.ftc.gov/system/files/documents/public_statements/1598063/negative_option_policy_statement-10-22-2021-tobureau.pdf.

¹²⁸ The CFPB has taken similar steps, including issuing a circular in January 2023 stating that deceptive designs used by companies to confuse and deceive consumers into enrolling in subscription services via negative option marketing may violate the prohibition on unfair, deceptive, or abusive acts or practices (UDAAP) in certain instances and taking action against companies that have employed such practices. See Consumer Financial Protection Bureau, “Consumer Financial Protection Circular 2023-01, Unlawful Negative Option Marketing Practices,” January 19, 2023, www.consumerfinance.gov/compliance/circulars/consumer-financial-protection-circular-2023-01-unlawful-negative-option-marketing-practices.

¹²⁹ United Kingdom Department of Business, Energy & Industrial Strategy, “Reforming Competition and Consumer Policy. Driving growth and delivering competitive markets that work for consumers,” 2021, assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1004096/CCS0721951242-001_Reforming_Competition_and_Consumer_Policy_Web_Accessible.pdf.

¹³⁰ See Australian Competition & Consumer Commission, “Digital platform services inquiry. Interim report No. 3 - Search defaults and choice screens,” September 2021, www.accc.gov.au/about-us/publications/serial-publications/digital-platform-services-inquiry-2020-2025/digital-platform-services-inquiry-september-2021-interim-report. See also Australian Competition & Consumer Commission, “Digital platform services inquiry. Discussion paper for interim report No.5: Updating competition and consumer law for digital platform services,” February 2022, www.accc.gov.au/system/files/Digital%20platform%20services%20inquiry.pdf.

peer-to-peer (P2P) payment apps¹³¹ and BNPL apps, data privacy shortcomings have proved to be a common theme. The following suggest good practices for data privacy that could be put in place for the BNPL industry.

At a minimum, BNPL companies should be required to obtain active consumer opt-in for the collection of additional data that is not necessary for the core functioning of the service. CR's testing indicated that several BNPL providers already follow this practice, which could be made an industry standard.¹³² Active opt-in could also be required for third-party data sharing, rather than opting in consumers by default. BNPL providers should be required to provide more easily accessible means for consumers to control their privacy settings, and default privacy settings could be required to prioritize user privacy across the board.

Alternatively, stronger measures could be considered, in particular moving beyond a consent-based approach. For example, the EU General Data Protection Regulation (GDPR) requires that personal information be collected for explicit, specific, and legitimate purposes, regardless of consumer consent. A clear definition would be required for legitimate purposes. Data minimization and privacy-by-design requirements could be considered, which would limit the collection of data to what is necessary for the core function of the BNPL service (unlike current BNPL provider practices).

With respect to data harvesting, one further approach that could be explored is the treatment of alternative data or consumer-derived data. Applying certain data privacy standards to such data could help to provide consumers with more control over data harvesting practices.

Improved dispute resolution

BNPL providers should be required to develop clear processes to ensure the fast and efficient resolution of returns and payment disputes between consumers, merchants, and BNPL providers. The steps that consumers should take to initiate a dispute should be clear and clearly communicated to consumers. Extending provisions on chargeback rights from the Fair Credit Billing Act (FCBA) to BNPL loans, with appropriate adjustments as needed, would help to address several of the issues discussed in Section IV. For example, among other rights, chargeback rights would allow consumers to withhold payment temporarily while a complaint is being investigated.

Additional measures

Additional, discrete measures should be considered to address other problematic practices raised in Section IV. For example, BNPL lenders should be required to provide users with options to turn off automatic repay. The Electronic Fund Transfer Act (EFTA) prohibits a creditor from requiring a consumer to repay a loan through an automatic withdrawal from their deposit account. This prohibition could be

¹³¹ Consumer Reports, "Peer-to-Peer Payment Apps: A Case Study for a Digital Finance Standard," January 2023, advocacy.consumerreports.org/wp-content/uploads/2023/01/P2P-Whitepaper-Final-Report-1_24_23.pdf.

¹³² However, note that BNPL providers already seem to be skirting around this protection by defining in-app shopping experiences provided and consented to by the consumer, along with information collection that is part of these experiences, as "core" to the service. See Consumer Reports, "Buy Now, Pay Later: A Case Study for a Digital Finance Standard," May 2023, advocacy.consumerreports.org/wp-content/uploads/2023/05/Buy-Now-Pay-Later-A-Case-Study-for-a-Digital-Standard-1-2.pdf.

extended to BNPL loans. BNPL providers could also be prohibited or discouraged from using credit cards as a repayment mechanism.

With respect to late fees, policymakers could consider developing standards to ensure that late fees are reasonable. One approach would be to require that late fees be proportionate to the cost incurred by lenders for a missed payment, similar to provisions included in the Credit Card Accountability Responsibility and Disclosure (CARD) Act.¹³³ BNPL providers should be prohibited from charging multiple fees for the same missed payment. The industry should also work toward greater standardization regarding when late fees are applied, in order to lessen confusion among consumers. As noted previously, some BNPL providers have already begun taking steps in this direction, including eliminating or introducing caps on late fees.

Mechanisms for implementing recommendations

The above measures are intended to provide a broad menu for stakeholders to choose from, in order to provide the flexibility to address different aspects of the BNPL market as needed. Depending on the measure, different vehicles could be used for implementation. Some measures will require new rules, others will call for expansion of existing rules, while other measures may be better suited to guidance or instructions from policymakers. And other measures will call for enhanced supervision by regulatory authorities.

Some stakeholders have advocated for full application of current rules on credit and payments to be applied to BNPL, while others have argued that completely bespoke rules are needed. As the above suggestions illustrate, it may be preferable to instead craft a more nuanced approach, applying existing rules where appropriate and developing tailored rules where needed in order to maintain the benefits of BNPL while addressing risks in a targeted manner. While there are some aspects of BNPL that are unique to the product, many aspects of BNPL can be covered by extending or clarifying the application of existing financial sector regulation.

This appears to be the current path chosen in both the U.K. and Australia. In February 2023, the U.K. government published plans to regulate BNPL credit agreements.¹³⁴ The proposed plan combines applying current financial consumer protection rules on credit to BNPL while also developing new, tailored rules for certain topics. In brief, current rules on financial promotions, the content of credit agreements, and dispute resolution will be extended to apply to BNPL. Current rules on pre-contractual disclosures and creditworthiness assessments were determined not to be appropriate or proportionate for BNPL agreements in their current form, so tailored rules for BNPL will be developed for these topics.

The Australian government is pursuing a similar approach. In a recent speech in May 2023, the Assistant Treasurer and Minister for Financial Services announced that BNPL products will become regulated as credit products and will be required to comply with statutory product disclosure obligations, existing restrictions on unacceptable marketing, responsible lending obligations, and statutory dispute

¹³³ Note that it may be necessary to consider different business models within the BNPL industry. Where a model focuses on interest-free BNPL loans with relatively large late fees, it may be more appropriate to require that late fees be incorporated into APR disclosure rather than restricting such fees.

¹³⁴ HM Treasury, “Regulation of Buy-Now Pay-Later: Consultation on Draft Legislation,” February 2023, assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1136257/BNPL_consultation_on_draft_legislation.pdf.

resolution requirements. However, his speech noted that legislation would ensure that “*obligations on BNPL providers are scalable and technologically neutral*” and would seek to ensure “*the right fit for the risk level of [BNPL providers’] products.*”¹³⁵

The BNPL industry itself can play an important role in implementing many of the above measures. As noted in this report, for certain topics, some BNPL providers have begun introducing more responsible practices. Such trends should continue to be pursued as the market evolves in order to create higher standards across the industry and improve its reputation. In particular, the industry could work toward developing more consistent and standardized approaches in areas such as late fees and dispute resolution. In Australia, the Australian Finance Industry Association (AFIA) has developed a Buy Now Pay Later Code of Practice, which includes provisions on considering the vulnerability of customers, acknowledging complaints within one day and providing an initial response within 10 days, and charging late fees that are fair, reasonable, and capped.¹³⁶

¹³⁵ Australian Government Ministers Treasury Portfolio, “Address to the Responsible Lending & Borrowing Summit,” May 2023, ministers.treasury.gov.au/ministers/stephen-jones-2022/speeches/address-responsible-lending-borrowing-summit.

¹³⁶ Australian Finance Industry Association, “AFIA Buy Now Pay Later Code of Practice,” March 2022, afia.asn.au/files/galleries/AFIA_Code_of_Practice_for_Buy_Now_Pay_Later_Providers.pdf.

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