

Regulation of Buy-Now, Pay-Later: consultation on draft legislation
27/11/2024

Executive summary:

In response to this call for evidence on Buy-Now, Pay-Later by HM Treasury we call for the following policy recommendations

- ***HM Treasury or the Financial Conduct Authority (FCA) should develop specific pre-contractual requirements for BNPL products to help consumers better understand the credit nature of BNPL.***
- ***HM Treasury or the FCA should collaborate with BNPL providers, retailers and academics to design these pre-contractual requirements, ensuring they effectively raise consumer awareness about the credit nature of BNPL.***
- ***HM Treasury or the FCA must engage a diverse group of consumers, including vulnerable consumers, to participate in the design of pre-contractual requirements for BNPL products.***

Response authors:

[Dr Mee-Chi SO](#), Associate Professor of Business Analytics, at the University of Southampton, UK. Mee-Chi's research interests are consumer credit behaviour and consumer credit risk modelling. Mee-Chi has published her research in peer-reviewed academic journals, such as Decision Support Systems, European Journal of Operational Research, International Journal of Forecasting, Journal of the Operational Research Society, and Journal of Risk Model Validation among others. She also co-authored a review "Credit Card Market Literature Review: Affordability and Repayment" for the Financial Conduct Authority (FCA)' credit card market study.

Mee-Chi is working on the project entitled "*Unveiling the credit nature of Buy-Now-Pay-Later: The effect of disclosure messages*". **The result of this project provides evidence and policy recommendations in relation to the following questions:**

- **Question 1:** Do you have any comments on the proposed approach and/or drafting disapplying provisions on pre-contractual information (sections 55 and 55C)?
- **Question 2:** Do you have any comments on the proposed approach and/or drafting disapplying provisions on the form and content of agreements (sections 60, 61 and 61A)?

Response:

I agree provisions on pre-contractual information under sections 55 and 55C as well as the form and content of agreements under sections 60, 61 and 61A of the Consumer Credit Act (CCA), are largely irrelevant to BNPL agreements. Therefore, applying the current CCA pre-contract credit information (PCCI) provisions to BNPL agreements would likely disrupt customer journeys or cause confusion.

Nevertheless, I believe **there is a need to develop pre-contractual information requirements tailored specifically to BNPL products**. Through behavioural experiments, I examined the impact of presenting a BNPL disclosure statement at the pre-contractual stage online checkout. I also explored methods of presenting this statement to ensure consumers are better informed about both the benefits and risks of BNPL schemes.

Why is it important to develop a specific pre-contractual provision for BNPL products?

As a relatively new payment mechanism, consumers' understanding of BNPL varies significantly (FCA, 2021). BNPL is often marketed as a scheme that allows consumers to spread the cost over an interest-free period. However, the fact that BNPL is a credit product, which may involve late charges, is not prominently disclosed by most online retailers. Consequently, many consumers perceive BNPL as merely a convenient way to shop, aligning with their lifestyle and tend to use it more than they can truly afford.

This lack of clarity regarding the nature of BNPL can lead to overspending beyond one's affordability, jeopardizing financial well-being. As more consumers struggle to repay their BNPL debt, the issue becomes increasingly significant. The Consumer Financial Protection Bureau (CFPB, 2023) reports that the delinquency rates among BNPL users are higher than those of non-users. Similarly, Schomburgk and Hoffmann (2023) show that increased BNPL usage is associated with greater money management stress and, consequently, lower consumer well-being. The growth and widespread usage of BNPL, therefore, pose a wider societal challenge.

The use of BNPL may have a greater impact on vulnerable consumers. This group, characterised by relatively low credit scores and low income, is more likely to rely on point-of-sale credit (Salisbury and Zhao, 2020). Furthermore, under the current cost-of-living crisis, the number of vulnerable customers turning to BNPL may grow even further.

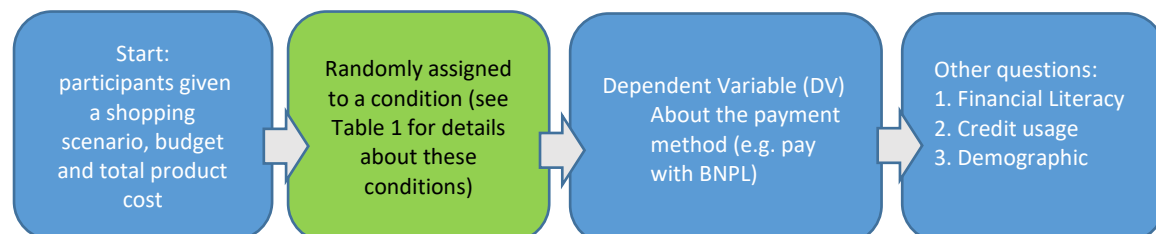
Implementing regulations that enforce clear pre-contractual disclosures about the credit nature of BNPL could help inform consumers, particularly those unaware of its credit implications. Such measures could reduce overreliance on BNPL and promote more responsible usage.

Why might pre-contractual provisions affect customers' payment decisions?

The effective use of disclosures or warning messages as intervention has been demonstrated in other areas, such as payday loan (Bertrand and Morse, 2011) and investment fund (Thorp et al., 2020). Most importantly, Adam and CogCo (2023) conducted behavioural experiments on a shopping platform to investigate the impact of disclosure statements on consumers' decisions to use BNPL. Their experiments showed that certain types of disclosure messages could reduce participants' likelihood of using BNPL.

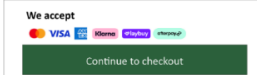
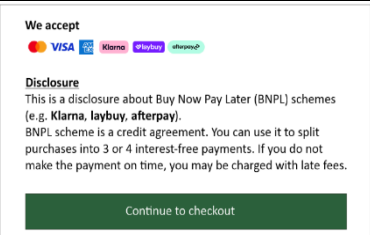
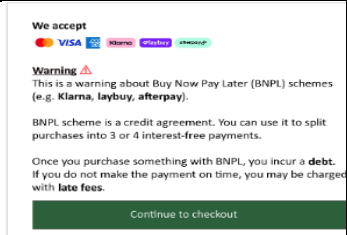
What was tested in my project about pre-contractual information?

Four behavioural studies were conducted as part of my project. In Studies 1, 2, and 4, participants were presented with a shopping scenario (e.g., purchasing an outfit for an event or shopping for the new season), along with a budget and the total product cost. They were then randomly assigned to one of several conditions, each featuring a different message, disclosure, or warning about BNPL. After reviewing the information, participants were asked to choose a payment method. Following the experiment, they answered demographic and financial literacy questions. The flow of these experiments is summarized below:



Study 3 aims to determine whether a specific version of disclosure is more effective in communicating the credit nature of BNPL schemes. In this experiment, participants were randomly

assigned to one of eight conditions 2(Format: Bullets, Text) x 2(Source: Financial Regulator, Not specified) x 2(Strengthen: Standard, Strong). Three examples of these conditions are presented in Table 1. After reviewing the disclosure provided, participants were asked to rate their responses to questions across four measures: Message Perception, Effect perception, Trustworthiness and Perception of warning.

Info.	Main research question	Quick overview on different conditions			Key outcomes
Study 1 No. of participants: 580. Options of the dependent variable: (1) Pay with BNPL (2) Shop Later	Does including a message with more information about BNPL influence participants' intention to use BNPL?	• Condition 1 (Standard): Buy-Now-Pay-Later (BNPL) is a new payment method. It allows consumers to pay over time without paying any interest. Klarna, Laybuy or Afterpay are some of UK's popular BNPL providers. • Condition 2 (Promoting BNPL): (same as Condition 1 and add the text listed below) BNPL providers often partner with retailers all over the world to provide a smooth, easy and safe way for consumers to buy what you love today. Using BNPL, you can choose to split purchases into 3 or 4 interest-free payments. A convenient way to shop for what you want at the time you need it! • Condition 3 (Credit Nature of BNPL) (same as Condition 1 and add the text listed below) Do you know BNPL is a form of credit? Once you purchase something with BNPL, you incur a debt. With most BNPL schemes, if you fail to repay any BNPL instalments, you will also need to pay late charges. A UK study found that one out of three BNPL borrowers say their BNPL repayments have become unmanageable. Moreover, the UK government will soon require BNPL providers to conduct an affordability check prior to any BNPL transaction.			• The “credit nature of BNPL” message influences participants’ payment decisions. • The “promoting BNPL” message does not affect participants’ payment decisions. • There is no clear difference in results for participants with varying levels of financial literacy.
Study 2 No. of participants: 330. Options of the dependent variable: (1) Pay with BNPL (2) Pay with Credit	Does including a disclosure or warning message about BNPL on the checkout page affect participants’	Condition 1 (Control) 	Condition 2 (Disclosure message) 	Condition 3 (Warning message) 	• Both disclosure and warning messages reduce participants’ intention to use BNPL. • There is no significant difference between disclosure and warning messages in influencing

Card (3) Shop Later	payment decisions?		participants' intention to use BNPL.						
Study 3 No. of participants: 387. Four Likert-scale measures as DVs: (1) Message Perception, (2) Effect perception, (3) Trustworthiness, and (4) Perception of warning	What features should be included in a BNPL message to enhance its effectiveness ?	There are eight different conditions in this study. Here I provide three of them as examples: <table><tr><th>Example Condition 1 (Regulator/Text/Standard)</th><th>Example Condition 2 (Not specified/Bullet/Strong)</th><th>Example Condition 3 (Regulator/Bullet/Strong)</th></tr><tr><td> We accept  Disclosure As required by the Financial Conduct Authority, this is a disclosure about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay). BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. If you do not make the payment on time, you may be charged with late fees. Continue to checkout </td><td> We accept  Warning ⚠ This is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): • BNPL scheme is a credit agreement • Split your purchases into 3 or 4 interest-free payments • Once you purchase something with BNPL, you incur a debt. • You may be charged with late fees for missed payments Continue to checkout </td><td> We accept  Warning ⚠ As required by the Financial Conduct Authority, this is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): • BNPL scheme is a credit agreement • Split your purchases into 3 or 4 interest-free payments • Once you purchase something with BNPL, you incur a debt. • You may be charged with late fees for missed payments Continue to checkout </td></tr></table>	Example Condition 1 (Regulator/Text/Standard)	Example Condition 2 (Not specified/Bullet/Strong)	Example Condition 3 (Regulator/Bullet/Strong)	We accept  Disclosure As required by the Financial Conduct Authority, this is a disclosure about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay). BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. If you do not make the payment on time, you may be charged with late fees. Continue to checkout	We accept  Warning ⚠ This is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): • BNPL scheme is a credit agreement • Split your purchases into 3 or 4 interest-free payments • Once you purchase something with BNPL, you incur a debt. • You may be charged with late fees for missed payments Continue to checkout	We accept  Warning ⚠ As required by the Financial Conduct Authority, this is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): • BNPL scheme is a credit agreement • Split your purchases into 3 or 4 interest-free payments • Once you purchase something with BNPL, you incur a debt. • You may be charged with late fees for missed payments Continue to checkout	• Bullet points do not have a clear effect. • Mentioning the FCA appears to have a stronger effect on participants' perception of the warning. • Messages positioned as “warnings” increase the effectiveness across all four measures.
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Study 4 No. of participants: 200 Options of the dependent variable: (1) Pay with BNPL (2) Pay with Credit Card (3) Shop Later	Does displaying disclosure or warning messages about BNPL on the checkout page change participants' payment decisions?	This study is similar to those of study 2. However, the conditions were chosen based on results in study 3. <table><tr><th>Condition 1 (Not specified/Text/Standard disclosure)</th><th>Condition 2 (Regulator/Text/Strong disclosure)</th></tr><tr><td> We accept  Disclosure This is a disclosure about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay). BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. If you do not make the payment on time, you may be charged with late fees. Continue to checkout </td><td> We accept  Warning ⚠ As required by the Financial Conduct Authority, this is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. Once you purchase something with BNPL, you incur a debt. If you do not make the payment on time, you may be charged with late fees. Continue to checkout </td></tr></table>	Condition 1 (Not specified/Text/Standard disclosure)	Condition 2 (Regulator/Text/Strong disclosure)	We accept  Disclosure This is a disclosure about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay). BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. If you do not make the payment on time, you may be charged with late fees. Continue to checkout	We accept  Warning ⚠ As required by the Financial Conduct Authority, this is a warning about Buy Now Pay Later (BNPL) schemes (e.g. Klarna, laybuy, afterpay): BNPL scheme is a credit agreement. You can use it to split purchases into 3 or 4 interest-free payments. Once you purchase something with BNPL, you incur a debt. If you do not make the payment on time, you may be charged with late fees. Continue to checkout	• There was no significant difference between the two conditions.		
Condition 1 (Not specified/Text/Standard disclosure)	Condition 2 (Regulator/Text/Strong disclosure)								
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Table1. Summary of the four studies

What is the key message of this project?

The results of my project (Studies 1 and 2) demonstrate that participants who were shown a BNPL disclosure message were less likely to choose BNPL as their payment method. These findings are consistent with the results reported by Adams and COGCO (2023). While I did not identify a specific version of disclosure that delivers a stronger warning about BNPL, testing different formats has provided valuable insights that could guide future research.

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