



To: HM Treasury

Response to: “Regulation of BNPL Consultation”

January 2022

Our casework experience in Australia shows that BNPL debts are causing or exacerbating financial hardship in substantially the same manner as detailed in the Woolard Review.

In Australia, as is the case currently in the UK, BNPL sits outside the laws applying to other credit products. In Australia the industry has developed a self-regulatory code. The code however does not cover all of the industry and is woefully inadequate in curbing the consumer harm that can arise from BNPL.

We urge the UK Government to put in place legislation that provides adequate safeguards. We are making the same argument to the Australian Government.

Questions about this submission

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ABOUT US

Consumer Action and Financial Counselling Australia are consumer groups based in Australia.

About Consumer Action Law Centre

Consumer Action is an Australian independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling (often referred to as debt advice in the UK), legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just marketplace for all Australians.

Consumer Action operates a free legal advice service for individuals and community workers, and a financial counselling advice service¹ for individuals in the state of Victoria. Consumer credit debt is generally the predominant issue people seek our advice on via both these services, with the associated debts often the leading factor pushing people into, or towards, financial hardship.

About Financial Counselling Australia

Financial Counselling Australia (FCA) is the peak body for financial counsellors. Financial counsellors work in not-for-profit community organisations and provide free and confidential advice and support to people experiencing financial stress. In Australia, financial counsellors are subject to a range of professional requirements including that they hold a Diploma of Financial Counselling, undertake a minimum amount of continuing professional development each year and abide by a Code of Ethical Practice.

¹ Our financial counsellors receive calls to the National Debt Helpline, which is a free service available to any in Australia dealing with debts.

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Glossary/Reference Guide

AFIA	Australian Finance Industry Association
Afterpay	The largest BNPL provider in Australia. In the UK, the company trades as Clearpay.
ASIC	Australian Securities and Investments Commission (the equivalent of the Financial Conduct Authority in the UK)
Australian Code	AFIA Buy Now Pay Later Code of Practice
NCCPA	<i>National Consumer Credit Protection Act 2009</i> The NCCPA does not apply to BNPL providers. The law covers other credit providers and amongst other things, imposes a licensing regime and requirements on licensees to lend responsibly.

1. Context for our Response

1.1 About this Submission

This consultation comes at a critical time, as the use of BNPL has continued to grow significantly over the last few years both in Australia² and in the UK (as set out at 1.6 in the consultation paper). In Australia, this growth has flowed through to financial counselling casework.

The legal status of BNPL products in the UK, as described in Chapter One, is extremely similar to that in Australia – that is, it is essentially unregulated credit.

The purpose of our submission is to share our experience in a regulatory environment that lacks legislated consumer safeguards for BNPL products, and where debts accrued from BNPL products are becoming an increasingly common, contributing to the hardship experienced by our clients.

A key difference in the Australia compared to the UK has been the emergence of industry self-regulation in the form of a code of practice (Australian Code). This was developed by the industry, partly in response to a federal parliamentary inquiry in 2019 that recommended this occur.³

This submission:

- explores the experience of industry-self regulation in Australia setting out why this is not adequate in addressing the harm that being caused by BNPL;
- includes some observations about other aspects of the operation of BNPL in Australia;
- makes suggestions about the design of proportionate regulation.

1.2 Legal status of BNPL in Australia is similar to the UK

Just as BNPL products fall outside the operation of the *Consumer Credit Action 1974* (CCA) in the UK, they also avoid regulation by Australia's equivalent consumer credit legislation, the *National Consumer Credit Protection Act 2009* (NCCPA). The NCCPA contains similar consumer protections and obligations on creditors to those that exist in the CCA in the UK and applies to arrangements that meet a similar definition of 'credit' to that found in the CCA.⁴

As in the UK, some BNPL providers in Australia charge fees, such as account keeping fees as well as late payment fees. They are able to do this without falling within the definition of credit as the NCCPA contains some limited exemptions to the definition of 'credit', which permit fees to be charged if they fall within certain limits.⁵ In many cases, the fees charged by BNPL providers in Australia appear to be specifically structured to charge the maximum possible while staying within the boundaries of these exemptions. Despite these fees, Australian BNPL providers still make

² '20-280MR ASIC releases latest data on buy now pay later industry' <https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-280mr-asic-releases-latest-data-on-buy-now-pay-later-industry/>

³ <https://www.abc.net.au/news/2020-09-03/buy-now-pay-later-regulation-fintech-senate-inquiry/12614068>

⁴ See s 3(1) of Schedule 1 to the NCCPA (Schedule 1 is also known as the National Credit Code).

⁵ See s 6(1) of Schedule 1 to the NCCPA.

significant revenue via the fees they charge merchants, which appear to average around 4% of purchases made, significantly more than most other payment platforms.⁶

Australia's corporate regulator, the Australian Securities and Investments Commission (ASIC), has some limited oversight of BNPL because it falls under a definition of 'financial product' contained in ASIC's enabling legislation.⁷ However, the powers ASIC holds by virtue of BNPL falling within this definition are limited to more general laws, rather than those specifically designed for credit.⁸

In short, this means that BNPL occupies a very similar position in relation to Australian law as it does within UK law – that is, credit laws generally do not apply to it.⁹

2. Evidence of Detriment in Australia

We note HM Treasury's view that the evidence base for potential sources of detriment remains limited. Based on what is happening in Australia, we expect this is only because the evidence has not been collected, rather than that the detriment is not occurring.

The empirical evidence of consumer detriment from BNPL in Australia is clear. Given the similar regulatory environments between our two countries and the similar growth in BNPL, it is likely that the experience of UK consumers will be much the same as that of Australian consumers.

2.1 ASIC Reports in 2018 and 2020

The strongest evidence of detriment in Australia comes from reports by ASIC in both 2018¹⁰ and 2020.¹¹ These reports analysed data from the BNPL providers and also surveyed consumers about their experiences. Relevant findings from the most recent report in November 2020 show that a large number of people experience negative outcomes from using the product.

- 21% of buy now pay later users surveyed had missed a payment in the last 12 months;¹²

⁶ In Australia, BNPL providers commonly prohibit merchants from passing on the fees charged by the BNPL provider on transactions, by the use of 'no surcharge rules'. While these arrangements appear to benefit consumers, there are signs that retailers aim to make back the costs incurred to consumers by other means, such as by inflating the retail prices of goods across the board, or where the agreed price for a product or service is negotiable. See example 3 in ASIC's Report 600 on BNPL:

<https://download.asic.gov.au/media/4957540/rep600-published-07-dec-2018.pdf>.

⁷ *Australian Securities and Investments Commission Act 2001* (Cth), s 12BAA.

⁸ ASIC also has a product intervention power that it can use to intervene regarding a financial product if there is a real risk that product is causing 'significant consumer detriment', however this power is intended to be a timely response to market wide conduct, and has only been used in exceptional circumstances to date.

⁹ The Australian Government has recently announced a consultation on the future of Australia's payment system and this will include BNPL. At present, BNPL falls outside of this framework, unlike other credit products. For more information, see <https://joshfrydenberg.com.au/latest-news/transforming-australias-payments-system/>.

¹⁰ Australian Securities and Investments Commission, Report 600, Review of buy now pay later, November 2018, <https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-600-review-of-buy-now-pay-later-arrangements/>

¹¹ Australian Securities and Investments Commission, Report 672, Buy now pay later: An industry update, <https://asic.gov.au/media/5852803/rep672-published-16-november-2020-2.pdf>

¹² *ibid*, p 12.

- 39% also had a small and/or medium amount credit contract (a small amount credit contract is colloquially known in Australia as a payday loan, a medium amount credit contract is a loan between \$2,000 - \$5,000 that is also a costly form of credit);¹³
- 20% of BNPL users reported that they had cut back or went without essentials (such as meals) in the last 12 months, in order to make their BNPL payments on time;¹⁴
- 15% of consumers had taken out an additional loan in order to make a payment on time.¹⁵

This detriment was magnified for younger people using BNPL who proportionately were more likely to have cut back on essentials in order to make a payment or to have taken out an additional loan, compared to other age groups.¹⁶

The analysis of BNPL data confirms the reliance of the business model on late fees:

- between 9% - 15% of BNPL transactions incurred late fees each month;¹⁷
- over the three year period to June 2019, BNPL revenue from late payment fees represented up to 15% of total revenue.¹⁸

A business model that relies so heavily on consumers paying a penalty in the form of a late fee is a cause for concern.

2.2 Financial Counselling Australia December 2021 Report

More recent data from the financial counselling sector reinforces the research from ASIC, demonstrating that harm from BNPL is becoming more widespread in Australia. In December 2021, FCA released a report on a survey of financial counsellors across Australia.¹⁹

The findings indicate that BNPL debt is growing rapidly in the case work of financial counsellors, often as an additional debt on top of other forms of credit such as credit cards and personal loans. Financial counsellors reported that it is common for clients with BNPL debt to become overcommitted with repayments, often across multiple accounts. Where 12 months ago, 31% of financial counsellors said that half, more or all of their clients had BNPL debts, this figure is now at 84%.

While this also coincides with a significant increase in the prevalence of BNPL generally, people only reach out to financial counsellors when they are in, or at risk of, financial hardship. It suggests a clear majority of people in such a situation have BNPL debts. As well, 61% of financial counsellors reported most or all their clients with BNPL debts are struggling to pay other living expenses.²⁰

¹³ *ibid*, p 12.

¹⁴ *ibid*, p 15.

¹⁵ *ibid*, p 15.

¹⁶ *ibid*, p 15.

¹⁷ *ibid* p 12.

¹⁸ *ibid* p 13.

¹⁹ It's Credit, It's Causing Harm and It Needs Better Safeguards: What Financial Counsellors Say About Buy Now Pay Later, Financial Counselling Australia, December 2021.

<https://www.financialcounsellingaustralia.org.au/docs/its-credit-its-causing-harm-and-it-needs-better-safeguards-what-financial-counsellors-say-about-buy-now-pay-later/>.

²⁰ *ibid*, p 6.

Responses from financial counsellors also indicated that their clients were using BNPL to pay for essential items (such as groceries), and risk being stuck in a cycle of debt. While some BNPL providers claim their products are not available for use on essentials, financial counsellors report that clients get around this at supermarkets by purchasing gift vouchers that can then be used there.²¹

3. The Australian Code does not Adequately Protect People

3.1 How the Australian Code fits into the regulatory landscape

As noted above, the BNPL industry in Australia has developed a Code of Practice (Australian Code) through their peak body, the Australian Finance Industry Association (AFIA). The Code came into effect on 1 March 2021.

The Australian Code falls well short of what consumers should be able to expect in terms of safeguards and rights when dealing with BNPL. While it is technically correct that the Australian Code goes above the law that applies to BNPL, this is an exceptionally low bar given that consumer credit laws do not apply to BNPL.

Consumer Action, Financial Counselling Australia and other consumer advocacy groups in Australia engaged with AFIA in the development of the Australian Code and provided feedback on draft versions,²² as we do with numerous industry codes. Unfortunately, most of our feedback was not taken on board.

There were no formal requirements imposed on AFIA and the BNPL sector by any government source in developing the Australian Code. The BNPL sector may have been encouraged to develop a code by the Australian Government, but industry has complete discretion on what the Australian Code actually says and does. Additionally, it has not gone through any formal government approval process, unlike other Australian financial services industry codes.²³

We point out the substantial holes in the Australian Code below as a warning of the likely outcome of industry self-regulation and to support the case for legislated proportionate regulation that can effectively mitigate consumer detriment. The Australian Code appears to be doing little to reduce the rate and severity at which BNPL debts contribute to financial hardship. We strongly recommend that the HM Treasury design regulation that legislates consumer protections as the best way to reduce the negative impact BNPL products can have on a substantial portion of people.

3.2 Not compulsory

Perhaps the most glaringly obvious hole in the Australian Code is that it is entirely optional. There are currently eight BNPL providers that are AFIA members and have signed up to the Code and publicly committed to be held to it. While they may represent a majority of sales in the market, this

²¹ *ibid*, p 9.

²² See, for example: <http://consumersfederation.org.au/wp-content/uploads/2020/05/20200506-FINAL-Submission.pdf>.

²³ For example, the Australian Banking Association submitted its Banking Code of Practice to ASIC for approval when it was last reviewed.

is only around half of the existing BNPL providers.²⁴ The Code has no application whatsoever to BNPL providers that are not signatories.

This also means that if in future the Australian Code was improved and a member didn't agree with it, they could just leave AFIA and elect to no longer be bound by the Code. While there may be reputational consequences, we suspect this reality probably contributed to the final Code being written in a way that seemed to aim to avoid needing any of the founding members to significantly alter their existing business models to be compliant. It will also likely discourage any material enhancements to the Code being made that do not suit the business interests of members in future.

3.3 Providers can offer credit without affordability assessments

The Australian Code's biggest shortcoming in terms of preventing financial hardship is the absence of any obligation on signatories, for the vast majority of BNPL products, to make any assessment as to whether the borrower can afford to repay the amount borrowed.

Clause 11 of the Australian Code's title refers to a commitment to make sure BNPL products are suitable for customers. Unfortunately, in substance, clause 11 is nothing more than an impressive exercise, taking over two pages, to say that BNPL providers need not do anything substantial except verify the identity of a customer before approving them for a line of credit up to \$2,000. If this relates to an existing customer of the BNPL provider, this limit is extended to \$3,000. This covers the lion's share of BNPL product structures and users.

Clause 11.3 contemplates BNPL providers undertaking an upfront assessment process and speaks about ensuring customers are not vulnerable and being satisfied with the information obtained about the customer. However, a close reading indicates these requirements do not actually require any specific action of the BNPL provider. In terms of affordability, customers need only be capable of making an initial payment upfront, and they are deemed appropriate borrowers.

Many BNPL providers promote the absence of any affordability assessment or credit check whatsoever in their marketing campaigns, and it is part of what makes BNPL so easy to access. This only changes if the BNPL provider is lending over \$2,000 (or \$3,000 to an existing customer) – at which point the Australian Code can be satisfied simply by an external credit check – to approve any amount up to \$15,000.²⁵ Only when approving BNPL transactions over \$15,000 are Code subscribers required to undertake any actual assessment of the finances of the customer.

This is in direct contrast to forms of equivalent regulated credit captured under the NCCPA, the key consumer protection regulation in Australia for credit. Under the NCCPA, credit providers must assess and verify the income and expenses of any prospective borrower and ensure the credit product is 'not unsuitable' before advancing them the credit (known in Australia as 'responsible lending'). The Australian Code goes to lengths to avoid establishing any obligation to lend responsibly.

This is a gaping hole in the Australian Code, and it is the main reason that it does little to nothing to reduce or prevent BNPL products sold under the Code contributing to financial hardship. We

²⁴ <https://www.ibisworld.com/au/industry/buy-now-pay-later/14769/> This report found that 17 BNPL providers were operational in Australia in April 2021.

²⁵ The Aus BNPL Code also allows BNPL providers to determine suitability with an assessment of the income and expenses of the borrower for amounts between \$2001-\$15,000, but the credit check appears to be the more commonly used option in these circumstances : see clause 11.5 and 11.12.

strongly urge the United Kingdom Government to address this significant issue in the BNPL playing field there.

3.4 BNPL providers are blind to financial hardship

We strongly agree with the Woolard Review finding that financial hardship is unlikely to be visible to BNPL providers. This is primarily a direct result of not assessing whether BNPL is affordable prior to approval. Where the provision of regulated credit (at least if following the law) requires the creditor to identify the other income and expenses of a prospective borrower, BNPL providers are likely to be unaware of what is going on in the background for their customers. While BNPL providers generally consider people making their BNPL repayments to be appropriate users of their product, these people may still be experiencing significant financial hardship

The inadequacy of the BNPL's approach to identifying financial hardship is evidenced by the vast discrepancies in the rates of hardship the industry has reported in Australia compared with those identified from other sources. For example, in 2020 AFIA told an Australian parliamentary committee that the incidence of hardship requests across the industry was less than one per cent.²⁶ This runs counter to the ASIC research from 2020, noted above, which found 1 in 5 users were experiencing harm.

As well, in the experience of financial counsellors, BNPL providers can be difficult to contact and do not respond appropriately to requests for financial hardship assistance. In the Financial Counselling Australia Report, financial counsellors were asked to rate the BNPL providers that they dealt with frequently, using a scale of 1 – 10, where 1 is the worst rating and 10 the best. Of the four providers rated, the ratings were: Afterpay 5.9,²⁷ Zip 5.5, LatitudePay 5.2 and Humm 4.7. These ratings indicate the industry has a long way to go to improve hardship responses.

3.5 The BNPL model incentivises prioritising BNPL repayments

While the approach of BNPL providers to freeze the accounts of customers who have missed payments and increase the spending limits of customers only in response to good payment history is described by industry as a mechanism for reducing financial hardship, there is data that suggests it can also encourage consumer behaviour that leaves them worse off. This is consistent with the observation in ASIC's 2020 report that customers use credit cards to pay their BNPL instalments.²⁸

In November 2021, the Commonwealth Bank of Australia provided data to a Parliamentary committee that indicated their customers who use BNPL products were 50-100% more likely to overdraw their transaction account, or fall behind on repayments.²⁹ Where 7.2% of customers with BNPL accounts had overdrawn their account, only 3.9% of similarly aged customers without BNPL accounts, had done the same.

A similarly concerning trend was highlighted in the Financial Counselling Australia Report, with many financial counsellors indicating that they had clients who prioritised their BNPL repayments over

²⁶ Senate Select Committee on Financial Technology and Regulatory Technology, *First Interim Report*, September 2020, at 8.63. Available at: https://parlinfo.aph.gov.au/parlInfo/download/committees/reportsen/024366/toc_pdf/SelectCommitteeonFinancialTechnologyandRegulatoryTechnology.pdf;fileType=application%2Fpdf.

²⁷ Afterpay is the inventor of BNPL. It operates in the UK, but under the name Clearpay.

²⁸ Buy now pay later: An industry update, ASIC, *Report 672*, p 17. <https://asic.gov.au/media/5852803/rep672-published-16-november-2020-2.pdf>

²⁹ <https://www.businessinsider.com.au/commonwealth-bank-bnpl-regulation>.

other essential expenses. The BNPL model can create an additional incentive for consumers to make their BNPL repayments – it keeps their account open, and can lead to purchase limit increases. This is reminiscent of practices in the credit card industry, since banned in Australia, where banks provided unsolicited credit card limit increases. In contrast, some BNPL providers automatically increase a consumer’s BNPL limit.

Being more lenient to people who miss payments is not a good solution to this issue – it can only be prevented by reducing the number of people that get to this point. Introducing an obligation for BNPL providers to have an understanding of a person’s financial situation before signing them up to their products, or increasing spending limits, is the obvious and best solution to these issues. BNPL providers are contributing to the debts of their customers, and it is essential that there is an **obligation on BNPL providers to understand the financial situation of their customer before deciding** to add BNPL repayments to their expenses.

Case Study – Donna’s story

Donna (name changed) is a single mother of three living in regional Victoria who works part time and receives a variable income. Donna contacted the National Debt Helpline in March this year because she was struggling to manage debts accrued from utility bills, a car loan, a credit card, insurance and multiple BNPL debts. The BNPL debts were all with companies subject to the BNPL Code.

Donna told us that she had recently obtained a loan from a third tier lender to pay off the credit card and some of her BNPL debts, because she was struggling to meet the repayments. Initially, Donna indicated that she was comfortable with her remaining BNPL debts. In the following months while we were assisting Donna negotiate some of her debts, she informed us that she was struggling for money and had been using BNPL to pay for food, and had to take out other short-term credit to pay for her daughter’s living expenses (which was likely provided in breach of credit laws).

Donna had high credit limits for BNPL products. At one point she owed \$2,000 to one major BNPL provider, nearly another \$2,000 to another BNPL provider, with a similar amount owing to the same provider via regulated credit as well. She likely had high BNPL credit limits because she had consistently made her repayments, which disguised her financial hardship. The reality was that she couldn’t afford the repayments with her other debts and was using these services to pay for essentials.

Donna is still paying off her BNPL debts, but has told us she cancelled one of her BNPL accounts. We have sought to assist her to negotiate the debt with the other BNPL provider, but this is difficult because so few laws apply to BNPL. Initially, the BNPL provider refused to provide Consumer Action with any documents regarding the BNPL debt (a likely breach of the BNPL Code). The BNPL provider described the BNPL facility as ‘not regulated’.

Regulation also cannot wait for open banking to be in a position to facilitate real time affordability assessments. In Australia, the technology is already available for open banking, but take up has been slow by industry. To tie the reform of BNPL to this process would incentivise the BNPL industry to drag its feet on its uptake. Consumer protections need to come first.

3.6 No assessment of affordability makes late fees more likely

As also set out in the Woolard Review and Consultation Paper, one other obvious way BNPL can contribute to financial hardship is through the fees charged for missed payments. The risk of this occurring is greatly exacerbated where BNPL providers do little to assess whether the customer has the capacity to repay the debt in the first place. If a person cannot afford the repayments in the first place, they are being set up to fail, and inevitably will incur late fees that mean they pay more for their purchases. These fees are more likely to be incurred by precisely the people who should not have been signed up to additional credit in the first place.

This also relates to another shortcoming of the Australian Code, which is drafted in extremely general terms. This makes interpreting the practical impact of the provisions a difficult task, and one that likely leaves BNPL providers with ample wriggle room.

One example of this is in clause 10.1(g) of the Australian Code. This says that late fees will be fair, reasonable and capped. This is vague and does not offer a commitment of real value. In terms of fair and reasonable, there is no point of reference for what this means. By comparison, the Australian Customer Owned Banking Code of Practice clarifies that similar fees will be reasonable, *having regard to their costs*.³⁰ While companies like Afterpay may claim that their flat \$10 late fee is reasonable, it seems far less reasonable when you consider that it is imposed regardless of the payment missed. For example, financial counsellors have reported customers paying \$10 late fees on repayments of \$8.

The same criticism can be levelled at the commitment to cap late fees – what value is a high cap? In Australia, Afterpay cap their late fees at 25% of the total value of the goods being purchased³¹ – this is still a substantial amount to pay on top of the original purchase cost. Latitude, another Code signatory, does not seem to indicate what, if any, cap applies to their late fees.³²

Section 4 of this submission includes further comments about the actual cost of BNPL.

3.7 No detailed approval process increases risk of vulnerabilities being missed

Case Study – Sophia’s story

Sophia called the financial counsellors at Consumer Action in June 2021. Sophia told us that she is very overwhelmed and is a survivor of family violence. She has approximately \$30,000 in debts, including a car loan, BNPL debt and 3 credit cards all in her name but incurred by her ex-partner. The BNPL debt is approximately \$4,000 and she originally took it out for dental bills. However, Sophia’s ex-partner has repeatedly used the account to buy things and does not make repayments. Sophia has now received a default notice from the BNPL provider.

Under the NCCPA, regulated credit providers must ensure any credit product sold is appropriate to the requirements and objectives that have caused the consumer to seek credit. This process provides a valuable point at which credit providers can identify vulnerabilities of a consumer. When

³⁰ <https://www.customerownedbanking.asn.au/storage/cobcop-jan-18-version-12-1634019447JaAF1.pdf>, clause 5.2

³¹ <https://www.afterpay.com/en-AU/terms-of-service>, accessed 7 December 2021.

³² <https://www.latitudepay.com/customer-terms-conditions/latitudepay-february-2021/> accessed 7 December 2021.

done correctly, making the necessary inquiries as to the purpose of the credit can help identify red flags that may indicate financial abuse. Coerced debt is a common factor in the inability for victim survivors to leave a violent or abusive relationship and re-establish their lives.

As noted above however, the Australian Code effectively allows BNPL providers to lend up to \$15,000 while being completely blind to the reason for which their customer is using the funds. This makes it the easiest form of commonly available credit that can be used to perpetrate financial abuse.

Obviously, a product that almost exclusively involves remote transactions may have limits on the extent to which it can be used to proactively identify financial abuse. However, this distinction with BNPL from regulated credit is one clear situation where BNPL makes accessing credit, and loading someone else up with the debt, even easier.

3.8 Returning products

The Australian Code is completely silent on any procedure or forms of assistance BNPL providers need to offer if there are problems with an item or service purchased using a BNPL product, despite being the intermediary between purchaser and retailer. It also means that by using BNPL, people have fewer rights or options available to them than if they used an alternative payment method, such as a credit card that has a chargeback option.

There is already one example of the impact this can have in a published decision by the Australian Financial Complaints Authority (AFCA), Australia's external dispute resolution service for financial services.³³ In that case, a customer used an Australian Code signatory's service to make a purchase, but within a week sought a refund as he found the product was faulty. The retailer apparently initially agreed to refund him, then reneged. Despite the BNPL provider having a relationship with the retailer, they indicated they could not help and continued to seek payment. The customer disputed the payment at AFCA and was unsuccessful, eventually being charged an additional 23% of the purchase price in late fees, as well.³⁴

3.9 Lack of Meaningful Enforcement Powers

A further shortcoming of the Australian Code is that the incentives for BNPL providers to comply with the meagre consumer protections it contains, are lower than under the consumer credit laws BNPL is designed to avoid. If a BNPL provider is found to have breached the Australian Code, they are only required to take the necessary action to fairly reinstate the consumer. The committee overseeing the Australian Code has sanction powers, but they are weak.³⁵

In terms of financial penalty, the committee's powers are limited to requiring the BNPL provider to undertake a commercially reasonable rectification process. There may also be costs involved if directed to undertake a compliance review, but nothing beyond that is necessary to identify the extent of the provider's non-compliance. All other sanctions only pose reputational risk for the BNPL provider, such as a notice of non-compliance being published. To date, we are not aware of any

³³ One of the few substantial benefits to the Aus BNPL Code is that it requires members to become members of AFCA – which is otherwise not compulsory for BNPL providers. However, as the Discussion Document already indicates that BNPL providers are required to make external dispute resolution available to customers, we assume it would provide little value in New Zealand.

³⁴ <https://service02.afca.org.au/CaseFiles/FOSSIC/711283.pdf>

³⁵ Australian Code, clause 10.9.

outcomes of inquiries, investigations or compliance activities of the committee overseeing the Australian Code.

In contrast, consumer credit laws have teeth, because they carry significant financial penalties if breached, and provide stronger protections that can be relied upon by consumers in external dispute resolution. BNPL services are capable of causing equivalent harm to individuals, and there is no reason their providers should not face the same penalties as other credit providers when they breach community expectations.

3.10 Questionable Marketing and Advertising

While the Australian Code contains a commitment that advertising and promotional material will be clear and not misleading and deceptive, BNPL providers in Australia continue to try and differentiate themselves from the provision of credit, and in a way that appeals to young people in particular.

A recent report from Newcastle University found that young people in particular did not initially recognise that using BNPL was using credit – with this realisation only coming after they struggled to make repayments.³⁶

BNPL websites and apps clearly include marketing materials aimed at associating their products with aspirational lifestyles that would not otherwise be available, and use technology to personalise the experiences for consumers. BNPL product app interfaces and tools also replicate the experiences of a digital game, giving people a sense of control and using rewards or positive reinforcement. We encourage the UK Government to consider that the current marketing of BNPL companies is helping foster an attitude to their products that encourages spending and plays down the risks associated with BNPL.

4. Other Observations from Australia

4.1 BNPL can be a high cost option

One of the myths surrounding BNPL is that it is an inexpensive form of credit. This is not true and depends on how the product is used. For the portion of people that pay fees, the cost of BNPL can be equivalent to that of high cost credit cards. For smaller amounts, the cost can be even more.

The example below, based on the Clearpay business model shows this. The example assumes that the consumer pays a late fee on all of the four payments.

Transaction amount	£70 (The Consultation Paper notes that average BNPL transactions are between £65-£75 – see 2.11)
Late fees	£6 per payment and capped at 25% of the purchase price or £36 whichever is less. ³⁷

³⁶ Farrugia, D., Cook., J Senior, et al., *Young people, debt and consumer credit pilot study report*, 2021, University of Newcastle, <https://nova.newcastle.edu.au/vital/access/manager/Repository/uon:38627>

³⁷ Clearpay UK website, <https://help.clearpay.co.uk/hc/en-gb/articles/360026261512-Is-there-a-cost-for-using-Clearpay->

Timeframe	“Shop now and pay over 6 weeks”. ³⁸
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The quasi annual interest rate for the example above is 28.25%.³⁹

If a BNPL provider charges both late fees and monthly account keeping fees, the quasi annual interest rates are much higher.

4.2 BNPL Business Models and Harm in Australia

There are a range of different BNPL business models and concerning practices in BNPL in Australia. We set these out below for the sake of completeness. In some aspects they reinforce the findings of the Woolard review. They also demonstrate how a loophole in the law can quickly become a gaping hole:

- A number of BNPL providers market BNPL for purchases of between \$15,000 - \$30,000. The first business models with these larger limits were for roof top solar panels, batteries and home renovations.⁴⁰ You can now however also use BNPL for health care, including cosmetic surgery.
- BNPL can be used to purchase fractional property investments.⁴¹ This is a complex investment product at the best of times;
- BNPL providers encourage people to use it for household bills, such as electricity, and everyday living expenses, such as groceries and food and beverages in pubs⁴². Using credit for day to day expenses can be a recipe for disaster. As well, people struggling to pay these expenses generally have other options such as accessing energy retailer hardship programs;
- BNPL debts being paid from credit cards
- Financial counsellors report more and more people with multiple BNPL accounts and payments. This actually makes it harder to manage money.

5. An Appropriate Regulatory Response and Conclusion

5.1 A Regulatory Response

Relying on self-regulation of the BNPL industry through a self-regulatory code is woefully inadequate. An appropriate regulatory response needs to include legislated requirements that:

³⁸ Clearpay UK website, <https://www.clearpay.co.uk/en-GB/how-it-works>

³⁹ Effective annual interest rate = $(1 + i/n)^n - 1$, where i = nominal interest rate, n = number of compounding periods.

⁴⁰ See for example: Brighte (www.brighte.com.au), Openpay (www.opy.com.au), Payright (www.payright.com.au)

⁴¹ See Bricklet (www.bricklet.com.au)

⁴² <https://thenewdaily.com.au/finance/finance-news/2021/11/09/afterpay-pubs-alcohol/>

- require BNPL providers to assess whether a person can afford to repay any initial credit limit, as well as any increases in the initial limit. This assessment must be based on their financial position;
- prohibit unsolicited credit limit increases;
- require BNPL providers to make reasonable inquiries about the purpose for which their customers are seeking a line of credit through their product;
- require BNPL providers to record BNPL limits in the credit reporting system;
- limit the cost of late fees that can be charged to a customer (the level will need further analysis, but should relate to reasonable quasi interest rates);
- require BNPL providers to respond to financial hardship appropriately;
- have processes to allow consumers to charge back transactions where there are disputes about the goods purchased;
- are members of an external dispute resolution scheme (in the UK, the Financial Ombudsman Service; in Australia, AFCA)
- ensure that financial penalties that are already part of consumer credit laws apply equally to the sale of BNPL products, where relevant.

5.2 Conclusion

While it may escape legal definitions, BNPL is credit. It is used in the same way as other credit products and carries the same risks. Leaving BNPL unregulated places the interests of businesses over consumers.

There is sufficient evidence based on the last nine months in Australia to indicate that a BNPL industry code is not sufficient on its own as an alternative to regulation. The relationship between BNPL and growing financial hardship is clear.

We urge the United Kingdom government to learn from the problems in Australia and take steps to ensure that the industry is far better regulated, in a manner that puts consumers, particularly vulnerable consumers, first.