



COVERSHEET

Minister	Hon Dr David Clark	Portfolio	Commerce and Consumer Affairs
Title of Cabinet paper	Approval to release discussion paper: Buy-Now, Pay-Later – Understanding the triggers of financial hardship and possible options to address them	Date to be published	10 November 2021

List of documents that have been proactively released

Date	Title	Author
October 2021	Approval to release discussion paper: Buy-Now, Pay-Later – Understanding the triggers of financial hardship and possible options to address them	Office of the Minister of Commerce and Consumer Affairs
27 October 2021	Buy-Now, Pay-Later – Understanding the Triggers of Financial Hardship and Possible Options to Address Them: Release of Discussion Paper DEV-21-MIN-0218	Cabinet Office

Information redacted

NO

Any information redacted in this document is redacted in accordance with MBIE's policy on Proactive Release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

In Confidence

Office of the Minister of Commerce and Consumer Affairs

Cabinet Economic Development Committee

Approval to release discussion paper: Buy-Now, Pay-Later – Understanding the triggers of financial hardship and possible options to address them

Proposal

- 1 This paper seeks agreement to release for public consultation a discussion paper: *Buy-Now, Pay-Later – Understanding the triggers of financial hardship and possible options to address them*. This discussion paper is seeking feedback on the relative costs and benefits of Buy-Now, Pay-Later (**BNPL**) to consumers (including financial hardship), business and the wider economy. Specifically the paper is seeking feedback on:
 - 1.1 the benefits of BNPL for consumers, businesses and the wider economy;
 - 1.2 how the use of BNPL could trigger financial hardship for consumers – under what circumstances and at which points in the consumer journey financial hardship could occur;
 - 1.3 how the risks of financial hardship from BNPL could be addressed if BNPL exhibited certain desirable features;
 - 1.4 how an effective BNPL sector should be defined – I have proposed it is one where addressing the risks of financial hardship is balanced against the benefits of BNPL; and
 - 1.5 what options are available to achieve an effective BNPL sector, including regulatory and non-regulatory options, the costs and benefits of these options, and how effectiveness could be monitored and evaluated.

Relation to government priorities

- 2 The proposal to release this discussion paper relates to the Government's Child and Youth Wellbeing Strategy and on-going response to COVID-19.
- 3 BNPL can be a useful tool for many families to manage spending, such as at the beginning of the school year and provides an alternative to other forms of credit. However, I am also conscious that under certain circumstances and at specific points in the consumer journey, BNPL could create financial hardship, which in turn could contribute to household and child poverty.

- 4 The use of BNPL is also increasing and so could the risk of financial hardship. Following the lockdown in March 2020, data indicated a sustained increase in the use of BNPL. With the recent lockdowns, there has been a further increase in the use of BNPL as consumers shift to online shopping. I have asked my officials to continue monitoring the situation in light of the current Alert Level response to the Delta variant outbreak.

Executive Summary

- 5 BNPL is a relatively new, innovative and fast growing credit alternative in New Zealand, and is particularly popular for online purchases.
- 6 Unlike other forms of credit, BNPL gives consumers instant access to goods and services without incurring any upfront fees or interest charges or fees - unless instalments are missed. Instead of applying interest charges or fees (unless instalments are missed) to the consumer, BNPL providers earn revenue by applying a fee to the business offering BNPL.
- 7 While there are benefits from BNPL to consumers, businesses and the wider economy from BNPL as an alternative to other forms of credit, I am concerned that for some consumers the use of BNPL will be unaffordable and unsuitable, and could result in financial hardship. This hardship may be visible to providers, for instance when a consumer misses or is late to make a payment, or may be less visible because by paying BNPL instalments, a consumer forgoes essential goods and services.
- 8 The discussion paper I am proposing to release seeks public feedback on the relative costs and benefits of BNPL to consumers (including financial hardship), business and the wider economy and options for ensuring an effective BNPL sector – one where addressing the risks of financial hardship is balanced against the benefits of BNPL.
- 9 I consider that the biggest risk factor for consumers from BNPL is the lack of consistent affordability assessments. Other triggers for financial hardship include ineffective hardship policies and unreasonable missed and late payment fees and processes, which are further compounded by consumer psychology and the potential reliance on BNPL to purchase essential goods and services.
- 10 I am of the view that an effective BNPL sector should deliver long-term benefits to consumers by enabling confident and informed participation in a transparent, competitive and innovative sector. I think there are a number of desirable features which could be introduced to contribute to an effective BNPL sector, including consistent affordability assessments when making lending decisions.
- 11 I am seeking feedback on three options in this paper. The first is the continuation of the status quo – the BNPL sector could progress self-regulation independent of Government; the second is to establish mutually agreed standards between BNPL providers and government, with a monitoring role held by government to ensure sector compliance; and the third

option is regulation under the Credit Contracts and Consumer Finance Act 2003 (CCCFA).

- 12 The options will be evaluated by looking at how they contribute to effectiveness in delivery of good consumer outcomes, flexibility to evolve with the sector, and legitimacy of how well the option will be enforced.
- 13 Following public feedback on the discussion paper, I will instruct my officials to analyse submissions and propose policy options to address the triggers for financial hardship. I will return to Cabinet next year with a further Cabinet paper seeking approval to progress the preferred policy option.

Background

BNPL is a form of credit that enables consumers to acquire goods and services up-front and pay for them in instalments without paying interest

- 14 BNPL is a relatively new form of credit available to New Zealand consumers. It allows consumers to pay for goods and services at participating businesses, typically using a mobile app at the point of sale, either in-store or online. For a fee, the business is paid for a good or service by the BNPL provider, which enables the consumer to receive the good or service up-front. The consumer then pays the BNPL provider weekly or fortnightly instalments over a specified period.
- 15 Consumers may hold BNPL accounts with multiple providers. There are currently seven BNPL providers operating in New Zealand.
- 16 The popularity of BNPL appears to be increasing – according to transactional card data between 2019 and 2020, growth in BNPL increased by over 50 per cent, with reports suggesting that BNPL could outstrip credit card payments for online transactions by 2024. BNPL is popular with consumers under the age of 45, and with female consumers, and is increasing as a form of credit to purchase services such as dental treatment and vehicle repairs.
- 17 We understand that BNPL providers earn most of their revenue by charging businesses – though some revenue is generated by consumers when they fail to make an instalment (default fee). The models of BNPL are continuing to evolve and change with the entry of new BNPL providers and potential partnerships with banks and payment card network processors such as Mastercard and Visa.

BNPL offers benefits to consumers, businesses and the wider economy

- 18 I see a number of benefits from BNPL business models and credit offerings which are desirable to maintain:
 - 18.1 For consumers: BNPL can be an effective and low-cost way to spread the costs of purchases (including unexpected high-cost purchases like

dentistry), take advantage of discounts through bulk purchasing and demonstrate credit worthiness by successfully paying off a transaction.

- 18.2 For businesses: BNPL may generate additional sales from customers who may not be able to afford the full cost of goods and services at point of sale. Some BNPL providers have significant consumer reach, and can help businesses access new consumer markets.
- 18.3 For the wider economy: BNPL disrupts the credit market by providing consumers with a low-cost alternative to existing credit products, resulting in greater innovation and competition, and therefore greater choice for consumers.

Unlike traditional credit products, BNPL falls outside the scope of the Credit Contracts and Consumer Finance Act because it does not charge interest

- 19 BNPL differs from other forms of credit in that the consumer does not pay interest on the amount owed, and as a result BNPL is not regulated under the CCCFA. BNPL providers are therefore not required to carry out affordability and suitability assessments that apply to other forms of consumer credit.
- 20 The CCCFA allows me, in my capacity as Minister of Commerce and Consumer Affairs, to recommend the making of regulations which could declare BNPL (as a class of arrangements or facilities) as subject to the CCCFA.
- 21 The BNPL business model enables real-time transactions and is supported by either credit checks and/or ongoing repayment behaviour to assess whether a consumer can afford instalments. Given the real-time nature of BNPL, the application of the CCCFA would need to be carefully considered to ensure the benefits of BNPL are not lost, including consideration of appropriate exemptions.

I am concerned that for some consumers, use of BNPL can cause financial hardship

- 22 BNPL is a growing credit alternative which provides benefits in terms of competition and innovation, but I have heard concerns that BNPL is creating financial hardship for some consumers.
- 23 My officials and I have had a number of discussions with financial mentoring organisations. These organisations work to help New Zealanders who fall into financial difficulty to manage their debts and have emphasised that they are seeing increasing numbers of clients for whom BNPL makes up a concerning part of their debt portfolio. Financial mentors report that clients use BNPL across a range of products and services, including to purchase clothing and school gear, electronics, whiteware, dentistry and haircuts. Many of these clients do not view BNPL as a form of debt.
- 24 These organisations have indicated to me that consumers may face financial hardship from the use of BNPL in two main ways:

- 24.1 Hardship which is easily observable to the BNPL provider: where the consumer cannot make their BNPL repayment instalment. This will be evident when they miss or are late to make an instalment. They may then experience compounding hardship through the application of missed or late payment fees. The percentage of BNPL revenue generated by default fees was 26 per cent in 2020-21. Additionally, when customers use BNPL to purchase essentials regularly, this is likely to be an indicator of financial hardship. Centrix data covering around 35 to 40 per cent of the New Zealand BNPL market, suggests that in August 2021, 8.3 per cent of active BNPL customers were in arrears (late or missed payments). In comparison, around 7.9 per cent of personal loans and 4.2 per cent of credit cards were in arrears.
- 24.2 Hardship which is not directly observable to the BNPL provider: where the consumer pays instalments, but in doing so is unable to afford essential goods and services, or make other debt repayment obligations. For example, hardship may not be visible is where consumers use credit cards to pay their BNPL instalments. Information provided by some BNPL providers suggests that on average around 20 per cent of consumers use credit cards to pay for their BNPL instalments.
- 25 It is clear that BNPL can either be a contributing factor in financial hardship for some consumers, or can be an issue for consumers already experiencing hardship. According to a 2021 survey, 63 per cent of BNPL consumers were extremely or somewhat concerned about their level of debt compared with 38 per cent of the general population.
- 26 I am concerned that for some consumers under certain circumstances and/or at particular points in their BNPL consumer journey, the use of BNPL will be unsuitable and could result in financial hardship. This Government has worked hard to protect consumers from getting trapped in cycles of unaffordable debt. I want to ensure that recent credit reforms are not undermined through the expanding use of BNPL.
- 27 The concerns and harms identified are not unique to New Zealand – though the approaches to address the concerns and harms vary according to existing regulatory frameworks. For example, in Australia, BNPL providers adhere to the Australian Finance Industry Association BNPL Code of Practice which was implemented on 1 March 2021. It is an industry code that has been developed by industry, working with the government. The UK has also recently announced it will be regulating the sector.

BNPL providers are aware of some of the concerns related to financial hardship and have developed a draft industry code

- 28 The BNPL sector is developing an industry code to initiate jointly agreed minimum standards that BNPL providers will be held to. My officials and I have provided comment on this Industry Code, but am not satisfied that the draft goes far enough to protect consumers.

- 29 It is my view that the current iteration of the Industry Code focuses on minimising the risk of default, therefore protecting BNPL provider interests. I think that the Industry Code could go further to better address the triggers of financial hardship for consumers such as unaffordability. I also think greater enforceability mechanisms are necessary to ensure compliance with the Industry Code.

I am proposing to consult on the triggers of financial hardship from BNPL

- 30 The discussion paper seeks feedback on the circumstances or instances which cause some consumers to experience financial hardship from the use of BNPL. This will inform the development of options which address these triggers, to ensure that the features introduced do not inadvertently impede the benefits the sector offers.
- 31 To understand the issues, information has been sought from BNPL providers, (which has been provided in confidence) and financial mentoring services, as well as other data sources. Based on the initial analysis carried out by officials, I am of the view that the lack of comprehensive affordability assessment is the root cause behind some consumers experiencing financial hardship.
- 32 The lack of affordability assessment triggers financial hardship due to the lack of visibility of consumer income and expenses, including the extent, nature and timing of other expenses, at the time of account activation and at the point that credit limits are increased. This can mean that consumers are accessing BNPL credit that they cannot afford within their income, when balanced with their existing expenses.
- 33 This is of particular concern where consumers use multiple BNPL accounts, multiple consumers within a household rely on shared household income without awareness of each other's spending, or where a consumer's circumstances or income and expenditure change in a way that impacts their ability to afford instalments.
- 34 The other contributing triggers of financial hardship identified are:
- 34.1 ineffective hardship policies and processes, which do not provide sufficiently clear pathways to consumer redress; and
 - 34.2 missed and late payment fees, which compound the impact of being unable to make a payment by adding to the original cost.
- 35 The financial hardship consumers experience due to these triggers is compounded by consumers' focus on the affordability of the initial instalment, rather than the total cost. BNPL products are widely viewed as a payment method alternative, rather than a form of debt. This can encourage spending beyond the consumer's means.

- 36 Some consumers use BNPL to purchase their essentials. While in the short-term this may not indicate the BNPL product is unsuitable, over time the use of BNPL in this way shows a reliance on BNPL that is concerning and indicates that the consumer may be facing severe financial difficulties.

An effective BNPL sector should deliver long-term benefits to consumers by enabling confident and informed participation in a transparent, competitive and innovative sector

- 37 I want BNPL products to deliver long-term benefits to consumers, directly (through use of BNPL), and indirectly (through the competition and innovation that the BNPL sector promotes). Consumers who use BNPL should be confident and informed participants in a transparent, competitive and innovative BNPL sector.
- 38 Most importantly, BNPL should only be available to consumers who can afford it without facing financial hardship, and where it is suitable to their needs. In order to ensure this, providers should ensure BNPL has the following features:
- 38.1 affordability and suitability assessments that are consistent across BNPL providers to enable lending decisions which reflect the extent, nature and timing of the consumer's financial position, and ensure the product meets the needs of the consumer, including identifying consumers who may be in vulnerable circumstances;
 - 38.2 reasonable missed and late payment fees and processes; and
 - 38.3 thorough and effective hardship policies which require proactive engagement with consumers, I also want BNPL to encourage and enable consumers to demonstrate financial responsibility. To achieve this, consumers should have access to information which can inform their decisions, and BNPL providers could encourage the use of personal financial management tools and undertake responsible advertising.

Options to achieve an effective BNPL sector which delivers long-term benefits to consumers are outlined in the discussion paper

- 39 In order to deliver an effective BNPL sector, I am seeking feedback on the design, and the costs and benefits of three options. These options could be used to implement the features discussed above, in order to address the triggers of financial hardship.
- 40 To assess how effectively the options protect the interests of consumers and deliver long-term benefits, I am assessing the options against the following criteria:
- 40.1 effectiveness – in protecting the interests of consumers;

- 40.2 flexibility – to allow for the BNPL sector to continue innovating and competing with other credit products; and
- 40.3 legitimacy – to ensure credibility and trust.

Option one: Retain the status quo

- 41 Under this option BNPL would remain outside of the CCCFA and the sector can choose to develop and introduce a voluntary sector code, which may or may not address the triggers of financial hardship. The government would not have a role in development of any self-regulation, or a direct role in evaluation or monitoring.
- 42 Option one may not be effective, as providers do not have to address the triggers identified because there is no mechanism for enforceability and compliance. However this option supports flexibility, as it balances the benefits that arise from the sector with allowing the sector to continue to innovate and compete with other credit providers.

Option two: Government establishes appropriate incentives for BNPL providers to develop an industry code which addresses the triggers of financial hardship

- 43 Under this option the sector is incentivised to establish, maintain and comply with an industry code, which addresses the triggers of financial hardship identified, due to the prospect of regulation.
- 44 Standards will be mutually agreed by government and the BNPL sector, which would ensure that consumers are effectively protected whilst ensuring there is sufficient flexibility for the sector to innovate, evolve and promote competition.
- 45 In order to ensure legitimacy, this option would also incorporate an ongoing independent review of how BNPL providers are addressing the triggers of financial hardship and protecting the interests of consumers. The outcome of the review would then determine whether sufficient progress was being made on addressing triggers of financial hardship through an industry code. If the review determined that progress was insufficient, I could consider taking further action to ensure consumers are adequately protected.
- 46 As well as providing legitimacy to an industry code, a regular, independent review would effectively provide an effective monitoring and evaluation mechanism and help to identify how individual BNPL providers may need to improve their performance to ensure compliance with an industry code.

Option three: Apply CCCFA to BNPL

- 47 Under this option I could use the powers I have under the CCCFA to declare BNPL to be consumer credit contracts and thereby allow BNPL to be regulated under the CCCFA, with existing monitoring and enforceability mechanisms in place to support legitimacy.

- 48 Applying the CCCFA to BNPL products would likely require exemptions from certain regulations of the CCCFA to ensure that the BNPL sector continues to provide competition to existing lenders. This requires a balance of effectiveness and flexibility to sufficiently protect consumer interests without overreaching and making BNPL business models unworkable.
- 49 Parts of the CCCFA that I could consider applying to BNPL include:
- 49.1 lender responsibility principles – which could require lenders to undertake comprehensive affordability assessments at the point of account activation and when credit limits are increased, and assist the consumer to be reasonably aware of the full implications of making the transaction;
 - 49.2 protections against unreasonable fees – which establish reasonable limits on what consumers can be charged;
 - 49.3 unforeseen hardship protections – which enable consumers to seek changes to their repayment agreement when their circumstances change resulting in hardship; and
 - 49.4 disclosure requirements – which support consumers to make financially responsible decisions by providing information to consumers and encourage the BNPL sector to compete on those features which are disclosed.

Financial Implications

- 50 There are no financial implications from the release of the attached discussion paper.
- 51 Should the Government decide to regulate BNPL providers there will be costs to the Crown. These will vary depending on the options chosen.

Legislative Implications

- 52 The release of the discussion paper does not raise any legislative implications.
- 53 Should government decide to apply the CCCFA, either wholly or partially to BNPL, regulations will need to be drafted and introduced.

Impact Analysis

Regulatory Impact Statement

- 54 The Regulatory Impact Analysis panel at the Ministry of Business, Innovation and Employment has reviewed and confirmed that the discussion paper can substitute for an interim Regulatory Impact Statement. It will lead to effective consultation and support the eventual development of a quality Regulatory Impact Statement.

Climate Implications of Policy Assessment

- 55 The Climate Implications of Policy Assessment (**CIPA**) team has been consulted and confirms that the CIPA requirements do not apply to this proposal as there is no direct impact on emissions.

Population Implications

- 56 I do not expect there to be significant implications for specific population groups, such as those with disabilities, from the release of this discussion paper.
- 57 If one of the options included in the discussion paper is pursued in future, this could have greater impact on the typical users of BNPL such as women, people under 45 and individuals who are unable to access traditional credit products.
- 58 When evaluating options, I will instruct my officials to balance the positive benefits of access to low-cost credit for these consumers, with the risk of financial hardship that BNPL may pose to some consumers.

Human Rights

- 59 The options included in the discussion paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Consultation

- 60 The following agencies have been consulted on this Cabinet paper and the attached discussion paper: Commerce Commission, the Financial Markets Authority, the Department of Prime Minister and Cabinet and the Treasury.
- 61 My officials have also consulted industry stakeholders and financial mentoring organisations who have provided data and insights into the sector.

Communications

- 62 I propose to release:
- 62.1 the discussion paper in November 2021 for a six week public consultation;
 - 62.2 an accompanying media statement on its release; and
 - 62.3 a consumer survey targeted to users of BNPL, which reflects the questions included in the discussion paper.
- 63 If there are any changes to COVID-19 Alert Levels and subsequent lockdowns, I propose to extend the consultation period – for example by an additional four weeks – to ensure that there is sufficient consultation on the discussion paper and related materials.

- 64 I expect there will be some divergent views in response to this consultation. It is my understanding that for many consumers, BNPL is a useful alternative to traditional credit options. However, it is clear that for some consumers, BNPL can cause real financial hardship.
- 65 I expect BNPL providers to object to the view that BNPL debt is significant enough to cause material hardship for individuals. I can understand their point of view when you reflect only on individual BNPL purchases. However, it is important to consider BNPL debt in the context of regulated credit lending decisions and BNPL providers' lack of visibility of consumers' existing debts and expenses.
- 66 I also expect to hear from some financial service providers who are subject to CCCFA regulations about the disparity of BNPL providers being exempt from such obligations.

Proactive Release

- 67 I intend to proactively release a copy of this paper in whole within 30 business days of decisions being confirmed by Cabinet.

Recommendations

The Minister of Commerce and Consumer Affairs recommends that the Committee:

- 1 **note** that the Buy-Now, Pay-Later (**BNPL**) sector in New Zealand is rapidly growing and is not subject to credit regulations under the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**);
- 2 **note** that BNPL can provide a convenient low-cost alternative to traditional consumer credit products, but that there are some consumers who are at risk from financial hardship due to the triggers of financial hardship, which include:
 - 2.1 the lack of comprehensive and consistent affordability assessments;
 - 2.2 ineffective hardship policies and processes;
 - 2.3 missed and late payment fees and unreasonable processes;
 - 2.4 consumer psychology of focusing on the initial payment rather than the total cost of BNPL products; and
 - 2.5 the use of BNPL to purchase essential goods and services due to lack of suitability.
- 3 **note** that the attached discussion paper seeks feedback on:
 - 3.1 the benefits of BNPL for consumers, businesses and the wider economy;

I N C O N F I D E N C E

- 3.2 how the use of BNPL products could trigger financial hardship for consumers – under what circumstances and at which points in the consumer journey financial hardship could occur;
 - 3.3 how the risks of financial hardship from BNPL could be addressed if BNPL exhibited certain desirable features;
 - 3.4 how an effective BNPL sector should be defined –I have proposed it is one where addressing the risks of financial hardship is balanced against the benefits of BNPL; and
 - 3.5 what options are available to achieve an effective BNPL sector, including regulatory and non-regulatory options, the costs and benefits of these options, and how their effectiveness could be monitored and evaluated.
- 4 **agree** to the release of the discussion paper titled *Buy-Now, Pay-Later - Understanding the triggers of financial hardship and possible options to address them*, subject to any minor or technical amendments, in November 2021 for a six week public consultation, with the flexibility to extend this public consultation period if there are COVID-19 Alert Level changes;
 - 5 **invite** the Minister of Commerce and Consumer Affairs to report back to the Cabinet Economic Development Committee on the preferred policy approach to the triggers of financial hardship by mid-2022;
 - 6 **note** that the Minister of Commerce and Consumer Affairs will issue a media statement on the release of the discussion paper;
 - 7 **agree** that the Minister of Commerce and Consumer Affairs proactively release a copy of this paper within 30 working days of decisions being confirmed by Cabinet.

Authorised for lodgement

Hon Dr David Clark

Minister of Commerce and Consumer Affairs