

Submission to HM Treasury Consultation on Regulation of Buy-Now Pay-Later

To Buy-Now Pay-Later Consultation Team,

My Background

I am a British Economics PhD Candidate & MBA at the University of Chicago Booth School of Business. I have been awarded the National Bureau of Economic Research (NBER) Dissertation Fellowship on Consumer Financial Management and my research is also supported by Chicago Booth's Fama-Miller Center for Research in Finance and George J. Stigler Center for the Study of the Economy and the State. My research focuses on the topics of household debt and credit information.

I have written the first published, academic economics research on the Buy Now Pay Later market – research supported by the Economic & Social Research Council (part of UKRI: UK Research & Innovation).¹ I have given media interviews on the BNPL market including with the Financial Times. I have also been on panels at Harvard, Federal Reserve Bank of Atlanta, and the RAND Foundation discussing the BNPL market with market participants, academics, and regulators.

Before moving to Chicago, I spent six years conducting economic research informing financial regulation at the UK Financial Conduct Authority (FCA), Bank of England, and Federal Reserve Bank of New York. I am a graduate of the University of Warwick & University College London. While at the FCA, I undertook research on the effects of payday loans on consumers, conducting field experiments testing policies to reduce credit card debt, the role of creditworthiness assessments and credit information, and created a consumer credit file panel as a standing data asset within the FCA and the linking of the Understanding Society household panel survey with credit file data.

For more details on my academic and policy research please see my website:

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I have no conflicts to declare.

¹ Guttman-Kenney, Firth, & Gathergood (2023) Buy Now, Pay Later (BNPL)...On Your Credit Card *Journal of Behavioral and Experimental Finance*, 37: 100788. <https://doi.org/10.1016/j.jbef.2023.100788>

Guttman-Kenney (2022) Buy Now, Pay Later...On Your Credit Card: A New Way Of Putting Off Payments. *Op-ed in The FinTech Times* <https://thefintechtimes.com/buy-now-pay-later-on-your-credit-card-a-new-way-of-putting-off-payments/>

Consultation Response

The proposed regulation would create a significant loophole that provides an opportunity for regulatory arbitrage. This is undesirable as would be expected to distort competition in the consumer credit market and poses a risk of consumers being unprotected.

Under the proposed legislation buy now pay later (BNPL) products offered by *third-parties* would be regulated. However, *merchants* who offer BNPL (or BNPL-esque) products would be unregulated despite such credit agreements performing the same economic function and even potentially having identical product structures.

The proposed legislation is disproportionate as it does not adjust for firm size. Why should a large merchant such as Amazon that offers a BNPL product that is economically identical to that offered by a third party be regulated differently? The product structures and potential need for consumer protections are the same. Economically they are the same and so should be regulated consistently.

The idea of merchants rather than third-parties offering BNPL-esque products is not an abstract hypothetical. Amazon recently ended its exclusivity deal with one BNPL lender.² It there seems very feasible for it, or other large merchants to offer their own BNPL-esque products in the not distant future. These are large firms and larger than many firms offering regulated forms of credit under existing legislation.

To address this, I recommend that the government amends the proposed legislation in the following way.

1. It should include in regulation both credit agreements offered by merchants and agreements offered by third parties.
2. Only exclude from regulation credit agreements offered by merchants whose total turnovers are classified as small or medium sized enterprises (SMEs) under the government's own definitions.³ Such regulation could be proportionally defined to exclude (i) micro and small businesses or (ii) also exclude medium-sized businesses.

This approach offers a proportionate approach to regulation. It prevents large merchants avoiding regulation. It prevents BNPL lenders facing unfair competition from such unregulated merchants. It is highly unlikely these large merchants would stop offering such products as doing so would decrease their customer base's demand to smooth payments and they are large enough to absorb regulatory costs. It is also proportionate as it avoids small merchants being affected by the regulation.

² <https://www.paymentsdive.com/news/affirm-amazon-buy-now-pay-later-payments-sole-bnpl-provider/641786/>

³ [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/757852/SM E HMT Action Plan Web Format Nov 18 PDF.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/757852/SM_E_HMT_Action_Plan_Web_Format_Nov_18_PDF.pdf)

The BNPL market has rapidly evolved in a short space of time with lots of innovation. The product structures offered by lenders have changed and non-BNPL lenders have started offering BNPL-esque products such as splitting up debit and credit card transactions and offering revolving credit facilities. Regulation of this market therefore needs to be designed to be forward-looking to ensure a consistent, proportionate approach to consumer protections and facilitate a competitive environment not distorted by regulation.

The nimbleness of the industry to incorporate new technological developments and develop new products is in stark contrast to the slow UK legislative process. The Financial Conduct Authority recommended regulation of BNPL in February 2021 following investigation in 2020. It is now March 2023 and there is little prospect of this market being regulated until 2024 (at the earliest) given time for parliament to legislate, the FCA to consult, make rules, and to allow firms sufficient time to implement these. Such timelines mean that it is unrealistic to consider that if (or when) the market adapted, new rules expanding the scope of BNPL regulation could be quickly put in place. Another round of legislation in the future would be inefficient use of time for all involved. By bringing merchant agreements under FCA regulation now, it enables the FCA quickly adjust regulation proportionately as risks develop. It is crucial to design regulation now, that is forward-looking to address potential market structures arising later.

Finally, including a broader set of credit agreements within regulation is long overdue and would yield longer-term benefits for conduct regulation. Currently, regulated lenders are required to conduct creditworthiness assessments evaluating a consumer's ability to pay.⁴ Such assessments currently largely rely on credit reference agency data.⁵ A challenge in the current regulatory environment is that reporting to credit agencies is voluntary and, even if the FCA decided to mandate reporting it can only do so for regulated firms. This means that consumers have shadow, unregulated debt that has a negative externality for regulated firms making it difficult for them to evaluate how much debt a consumer has, their regular payments as important expenditure components, and whether they are up-to-date with payments. Including all credit products except those offered by small, merchants in regulation would enable regulated lenders to better assess credit risk and conduct more accurate creditworthiness assessments that would be expected to increase the efficiency of the credit market.

I would be very happy to discuss any of the above further. Please reach out to me: benedict@chicagobooth.edu if that would be useful.

Kind regards,

Benedict Guttman-Kenney

⁴ <https://www.fca.org.uk/publication/policy/ps18-19.pdf>

Also see my research for more details on creditworthiness assessments and evaluating the data available to use for these: <https://www.fca.org.uk/publication/occasional-papers/op17-28.pdf>

⁵ <https://www.fca.org.uk/publication/consultation/cp17-27.pdf>