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Consumer Policy Team
Ministry of Business, Innovation and Employment
Wellington

Re: Buy Now Pay Later: Exemption from the Credit Contracts and Consumer Finance Act's fee provisions – targeted consultation

When protected from default fees that reflect an unreasonable cost relative to the impact of their inability to pay, borrowers are at less risk of debts spiralling and substantial hardship. Buy Now Pay Later (**BNPL**) lenders should not have any exemption from the Credit Contracts and Consumer Finance Act (**CCCFA**) requirement to not charge unreasonable credit or default fees relative to the transaction.

FinCap welcomes the opportunity to comment on the *Buy Now Pay Later: Exemption from the Credit Contracts and Consumer Finance Act's fee provisions – targeted consultation* (**Consultation Paper**) but is very concerned at the targeted one-week consultation process. We request that the Minister and Ministry of Business, Innovation and Employment (**MBIE**) cease running limited consultations of public interest, with short timeframes and no opportunity for the wider community to consider and share their views.

FinCap strongly opposes the proposed exemption in the Consultation Paper that is being considered and any other exemption. Financial Mentors continue to see issues with Buy Now Pay Later (**BNPL**) lending default fees causing or compounding substantial hardship. The *Commerce Commission vs Sportzone Motorcycles Ltd and MTF Ltd* judgement clearly points to issues around fairness when default fees are applied on an average rather than transactional basis.[1]

Instead, FinCap again recommends the Minister remove exemptions from the CCCFA requiring reasonable affordability and suitability checks for BNPL lenders. We also again recommend that the Minister use CCCFA 137A powers to apply all CCCFA requirements to lending by telecommunications companies that is currently uncaptured but causing harm.

There are consumer protection gaps with weak requirements for fair debt collection conduct and insufficient enforcement tools and visibility around unfair debt collection. This is a major issue as many more whānau face financial difficulty that will ripple for years in current economic conditions. FinCap again recommends that all debt collection activity be required to be accountable to financial dispute resolution schemes where not otherwise captured. We also repeat our recommendation that the Fair Trading Act be strengthened to clarify and provide appropriate enforcement mechanisms for fair debt collection conduct.

We expand on these comments in the submission below.

About FinCap

FinCap (the National Building Financial Capability Charitable Trust) is a registered charity and the umbrella organisation supporting the 185 local, free financial mentoring services across Aotearoa.

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[1] See for example, commentary at 105 in: https://comcom.govt.nz/__data/assets/pdf_file/0030/68826/Commerce-Commission-v-Sportzone-Motorcycles-Ltd-and-MTF-Ltd-Supreme-Court-Judgment-12-May-2016.PDF

These services supported over 69,000 whānau facing financial hardship in 2023. We lead the sector in the training and development of financial mentors, the collection and analysis of client data and encourage collaboration between services. We advocate on issues affecting whānau to influence system-level change to reduce the causes of financial hardship.

1. Do you have any views on the concerns raised by the BNPL provider

Financial mentors report many of the whānau they support being trapped in a cycle of servicing BNPL loans, even when the advanced amount and/or the default charges are unaffordable, to maintain a line of credit for food purchases. The borrowers start to see their access to a line of credit from BNPL lenders as their 'lifeline' for emergency credit and will avoid spending to repay other creditors or on the essentials to maintain access. Among other issues, this is increasing demand on food banks, a matter raised with FinCap by both financial mentors and a Cabinet Minister.

Because BNPL lenders, unlike others who must complete reasonable affordability checks, have been aggressively building a lending portfolio with limited regard to individual borrower's ability to repay, they appear to have chosen to accept a greater proportion of 'bad debt.' FinCap receives an insight report from the Centrix credit reporting bureau, which they may be able to share with MBIE. This regularly discloses that BNPL lenders who have reported have a far greater proportion of loans 90 days overdue than other types of consumer credit.[2]

The changes to see more appropriate lending protections around BNPL lending have been clearly on the horizon for years. We are confused as to why this issue has not been raised or worked through until just weeks ahead of a change that has been certain for a year. Financial mentors have continued to have their limited resources strained by the consequences of these under-regulated lending models throughout this time. Adjusting credit protections formulated over decades, or any delay to the planned implementation of CCCFA protections due to one provider's claim at this late stage, would reflect very poor process.

2. How effective would the proposed changes be in addressing the concerns raised by the BNPL provider?

If a significant proportion of borrowers have defaulted, this may reflect the risk that many were unable to afford the lending. BNPL lenders decided to take that risk when not completing sufficient affordability checks for the credit made available.

The change proposed for consideration will not solve the problem claimed by the BNPL lender and is not in the public interest. Firstly, the Consultation Paper notes changes could not be implemented by 2 September when the CCCFA is applied to this lending. This means the lender will need to comply anyway, even if the proposed changes are made.

Secondly, from a discussion with the Consumer Policy team, we understand that this lender has requested full exemption from being required to charge reasonable fees, to make their business viable. The proposed change to the underlying model for calculating reasonable default fees may just weaken the law and not improve their projections for viability.

The 'account freeze' on default implemented by both of the current prominent BNPL lenders seems to be an effective deterrent for non-payment. If the lender believes it needs unreasonable default fees to deter non-payment, this should be balanced against the insights from financial mentors outlined above. These are that borrowers will often prioritise repayments to ongoing access to BNPL lending facilities over anything else. We encourage MBIE to see if there are any relevant behavioural economics insights as to how the 'account freezing' feature of these lending products. We would have

[2] Centrix.(2024). *Credit Insights Report* July 2024, p.15

reviewed any research available with more time and will see if this is possible within a current project's scope.

3. How will the proposed changes impact BNPL borrowers? If so, how? Please provide examples.
The potential to charge default fees that are disproportionate to the loss in the context exposes borrowers facing hardship, who are not confident in requesting hardship assistance, to paying more and experiencing greater substantial hardship. This will ripple on to wider issues of other creditors not being paid, increased strain on borrower's mental health and increased child poverty to name a few.

Auckland University of Technology researchers conducted an online survey of 705 people aged between 18 and 34 about BNPL. One in six who used BNPL lending was unable to pay and incurred late penalties. One in five had forgone essential spending such as paying bills or buying food to cover BNPL payments.[3] Therefore, significant amounts of borrowers could end up facing further consequences in having paid default fees disproportionate to the loss they have caused. The paper noted that:

"*Financial mistakes made in early adulthood are difficult to undo, impacting current and future financial stability.*"[4]

We understand there are now just two main lenders making BNPL loans to borrowers currently. These lenders currently charge default fees against individual purchases rather than total amounts loaned.

It is common to have multiple purchases financed to one BNPL lender. Financial mentors and the borrowers they assist report relentless targeted marketing from these lenders applications to make multiple impulse purchases. This exposes the borrowers to significant fees where late payment across multiple purchases attract multiple flat fees.

One lender's current late fee setting also appears to allow it to unreasonably charge more than the total amount advanced in default fees within seven weeks, where that purchase is below $40. If someone had made many small purchases through this lender then they could, in a short period of time, end up owing far more in principal and fees than they would on another loan that is in no way exempt from CCCFA requirements. This is demonstrated in the table below through a hypothetical debt spiral situation where someone who borrowed $104.80, when only the initial $35 loan was affordable, ends up repaying $264.80. FinCap could likely source some actual statements for MBIE if provided more time to respond.

Hypothetical example – borrower unable to pay from 3 to 30 May 2024						
Purchase date	**Item**	**Advanced amount**	**Already repaid (1/4 per 2 weeks)**	**Fees for four weeks in default**	**Total owing within two months.**	**Total to repay**
5 April 2024	Shoes	$35.00	$17.50	$40.00	$57.50	$75.00
6 April 2024	Groceries	$19.50	$4.88	$40.00	$54.62	$59.50
21 April 2024	Meat	$37.80	$9.45	$40.00	$68.35	$77.80
2 May April 2024	Groceries	$12.50	$3.13	$40.00	$49.37	$52.50
Total		**$104.80**	$34.96	**$160.00**	$229.84	**$264.80**

[3] See: https://acfr.aut.ac.nz/__data/assets/pdf_file/0009/817803/FINAL-YA-Debt-Study-Industry-Report-v250823.pdf

[4]Ibid

How do late fees work?

Starting 31st July 2023, the late fee for Zip Pay in 4 will increase from $8 to $10 on new orders. If you miss a payment, you will see the new late fee of $10 added. This means for orders made from 12:00 AM NZST 31st July 2023, the new late fee amount of $10 will apply to any payments not received on or before their due date. The maximum limit for late fees per order will remain at $40.

Purchases made before 31st July will not be impacted by this change.

Orders with payments made on time will continue to not incur late fees.

We won't charge any fees or interest if you pay early or on time. If you do miss a scheduled payment, an $10 default fee is added to your account, and your spending will be paused until your overdue payments have been made. A further $10 fee is applied for every week the payment is unpaid.

Our fees are capped at $40 per order, but we really encourage you to get your payments up to date before this point. Being late on payments means that your details may be passed onto a collections agency and have your credit score negatively impacted.

Retrieved 30 July 2024 from https://help-nz.zip.co/hc/en-us/articles/5709472749839-How-do-late-fees-work

How much are the late fees?

Total late fees are capped at 25% of the order price, and will never exceed $68 per order, regardless of the order amount. There are slight differences for orders below and above $40:

- **For orders below $40:** the late fees charged will be capped at 25% of the total order value, never more;
  - For example, a $20 order with four $5 instalments will only ever incur a one-off $5 late fee.
- **For orders of $40 or above**: our model is slightly different. Each time an instalment is late, an initial fee of $10 is charged. If the instalment remains unpaid seven days after the due date, a further partial late fee (of up to $7) will also apply. This is the same for all late instalments until the 25% cap or $68 amount is reached.

We also pause your account until the balance is paid and you're back on track. We're committed to doing everything we can to help you not miss a payment. We've designed Afterpay to be completely different to traditional credit products that charge interest, so that our customers are never in a situation of high compounding interest and revolving debt.

Retrieved 30 July 2024 from https://www.afterpay.com/en-NZ/how-it-works

FinCap is unsure how the requirements around fees might or might not restrict merchant fees but sees it as a worthwhile potential impact for consideration. The proposed conditional exemption from two requirements around reasonable fees in individual situations might also permit increases to the hidden cost of credit in the merchant fees these BNPL lenders charge? FinCap's understanding is that merchants who make BNPL available are bound not to charge more to those using BNPL than those who do not purchase with BNPL. There may therefore be a risk, which needs consideration, that the exemption inflates prices for all consumers whether or not they use BNPL? This might just be a risk in general due to the way BNPL lending is structured?

4. What are the costs, benefits and risks of the proposed changes? Do you have any suggestions on how to mitigate any risks?

Benefits

Some financial mentors do acknowledge that a small cohort of borrowers they assist benefit from the availability of this form of credit. Generally, this is where they are only repaying one purchase at a time. If the claim by the lender is legitimate, then the change might increase the likelihood of this provider continuing to offer its services to borrowers. However, recent failure of other BNPL lenders indicates it is likely not the only factor in the viability of the provider.

The availability of this form of credit can also mean some whānau working with financial mentors have a faster and less intimidating alternative to interfacing with Work and Income for support. Although it should not be, approaching Work and Income for assistance can be ~~very~~ demoralising for many whānau, after decades of negative rhetoric about people receiving benefits and policies that have seen them intrusively scrutinised and judged, when in need of support. The culmination of debt to government can also lead to involuntary deductions to main incomes, which entrench hardship. However, the assistance from Work and Income is generally lower financial risk to these whānau, as there are no associated fees or interest rates.

Risk that would clearly present to financial mentors and of most concern to FinCap:

- The hidden hardship where borrowers prioritise paying unaffordable fees is worse than it would be without the exemption.
- The consequences of defaulting on loans that are not required to complete reasonable affordability assessments, are worse.
- Those uncomfortable or unaware of fee waivers will pay a poverty premium. Current BNPL lenders commit to reasonably helpful measures, like waiving fees when the borrower approaches them to disclose hardship. Financial mentors have found these effective, although comment it can be difficult for them to make contact to request the assistance.

  Ultimately those initially or totally without a financial mentor's support, without awareness of the hardship policies or without confidence in contacting the BNPL lender for assistance, will pay for other's defaults.
- The Centrix information referenced above shows a large amount of 'bad debt' arising from BNPL that could be passed on for debt collection. There is a current lack of clear requirement about reasonable debt collection fees or conduct in practice. An exemption could see borrowers who were not protected by affordability assessments paying excessive amounts for debt collection, including the averaged losses of other's non-payment.
- The current BNPL lenders that cap their default fees change their policies around this, or new lenders emerge within the exemption loophole whose model puts borrowers at even greater risk.
- Financial mentors and other community workers face more strain on their resources compared to the status quo of no exemption.

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Other risks for consideration:

- BNPL lenders are given an unreasonable competitive advantage over other lenders, that might not be in the interests of consumers.
- Borrowers and other lenders' confidence in the market through thorough regulation is eroded.
- The regulator may need disproportionate resource to monitor a different approach for how default fees are reasonably calculated at just two lenders.

5. Would you recommend any other approach to address the concerns raised by the BNPL provider?

The specific problem outlined is in relation to default fees. We oppose any exemption but also cannot see why the exemption would not be limited to just 44A of the CCCFA if progressed. An exemption to 41 of the CCCFA is much broader than the issue raised and creating a condition of the exemption in haste risks unintended consequences.

A stringent monitoring regime and regular review of the decision is needed if, despite our recommendation otherwise, the exemption is progressed.

6. Do you need to adjust your default fee policy to comply with the CCCFA fee provisions? If so, have you found ways to mitigate the potential negative impacts this adjustment might have on your business model and/or annual revenue? Please provide explanations and examples.
N/A

7. Will you consider making any changes to your default fee policy considering the proposed changes? If so, please provide explanations/examples.
N/A

Please contact Jake Lilley, senior policy advisor at FinCap on 027 278 2672 or at jake@fincap.org.nz to discuss any aspect of this submission.

Ngā mihi

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