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“Buy Now, Pay Later: No Fees. No Credit Check.”

Elaine Lee*

Abstract: Afterpay and Affirm, are financial technology (“fintech”) platforms that allow consumers to split their low-cost purchases into four installment payments—with seemingly no interest, fees, or hard credit inquiries. Similar to retailer fees on credit card transactions, these companies generate most of their profits as the intermediary between consumers and merchants. By flaunting celebrities like A\$AP Rocky and Keke Palmer, the loan products are heavily advertised as the “cool” alternative to traditional credit cards and are particularly well-received among Millennials and Generation Z (“Gen Z”) consumers. Consequently, consumer advocates are duly concerned that lenders irresponsibly extend credit to a young generation, who remain particularly vulnerable to the “present bias,” which undervalues future losses and overvalues present satisfaction. Currently, U.S. regulators have not confined lenders to proper regulatory parameters and remain silent on the regulatory gaps caused by the third-party lenders’ intentional “skirt[ing] of the definition of a [covered] loan under some U.S. laws.”¹

I. INTRODUCTION

Overnight, the COVID-19 pandemic shut down shopping malls and small businesses. With commerce being transitioned to online shopping coupled with Millennials and Gen Z consumers having limited access to credit, 'Buy Now, Pay Later' (BNPL) loans became a replacement to credit cards. Using the nationwide lockdown mandate as its impetus, a form of short-term, installment loans known as BNPL turned into a global phenomenon with over half of Americans having used the service by March 2021.² Analysts projected, at the end of 2021, consumers would have made nearly \$100 billion in retail purchases through BNPL arrangements, which is a fivefold increase from \$20 billion in 2019.³

Although this type of installment lending is widely touted as the next generation of finance, a similar provision of consumer credit can be traced back to the 19th century. At this time, Singer Sewing Machines

* This article initially started out as a final exam paper for a law school class, but now, Elaine Lee is an ardent voice of BNPL regulation.

¹ Stuart Condie, *'Buy Now Pay Later' Is Having a Moment as Pandemic Changes Shopping Habits*, WALL ST. J. (July 11, 2020), <https://www.wsj.com/articles/buy-now-pay-later-is-having-a-moment-as-pandemic-changes-shopping-habits-11594459800> [<https://perma.cc/JQ9M-REM7>].

² Ida Helene Grøtan & Mari Anette Hjorthol, *Consumers' Willingness to Incur Debt With "Buy Now, Pay Later" Payment Options*, BI NOR BUS. SCH. (Jan. 7, 2021), <https://biopen.bi.no/bitstream/handle/11250/2824333/2942473.pdf?sequence=1&isAllowed=y> [<https://perma.cc/6TK9-5DFF>].

³ Ron Shevlin, *Buy Now, Pay Later: The "New" Payments Trend Generating \$100 Billion In Sales*, FORBES (Sep. 7, 2021), <https://www.forbes.com/sites/ronshevlin/2021/09/07/buy-now-pay-later-the-new-payments-trend-generating-100-billion-in-sales/?sh=7f761e32ffe4> [<https://perma.cc/P4NW-5BLA>].

allowed families to rent sewing machines for a few dollars a month until they made their full purchase payment, at which point the families owned the machines.⁴ From then on, manufacturers implemented a business model that offered installment payment plans on big-ticket items, such as furniture, cars, or farm equipment, making their products more affordable.

When compared, BNPL loans are very similar to traditional consumer credit products. However, the borrowers utilizing BNPL loans are a critical difference and largely why BNPL has become such a prominent alternative to the credit card payment method. This is the case for two reasons—first, the targeted consumer demographic, and second, their deprivation from traditional credit platforms.

First, BNPL financial services primarily target and market their platforms⁵ to Millennials and Gen Z borrowers.⁶ This cohort of consumers displays different behavioral traits than prior generations. These behaviors are best encapsulated by the term of art, “millemmas,” which is loosely translated as the Millennial generation’s “big little problems that include the need for instant gratification.”⁷ A study showed that 40% of young consumers abandoned the bank account application process due to the length, the time-consuming nature of authentication, and the difficulty of the forms.⁸ Keying into the “millemmas,” the new BNPL products deviate from traditional credit cards, which typically involve longer applications and approval processes, by extending credit within a matter of minutes. This streamlined and convenient process often means that BNPL lenders do minimal credit checks (soft checks)⁹, or no credit check at all, so long as the consumer provides a valid phone number, email address and debit or credit card.

Second, in the aftermath of the 2008 financial crisis, Congress passed the Credit Card Accountability Responsibility and Disclosure Act (CARD Act) to tighten regulations around predatory credit extensions and

⁴ Tim Harford, *The Accidental Singer Sewing Machine Revolution*, BBC (Jan. 15, 2020), <https://www.bbc.com/news/business-50673541> [<https://perma.cc/K896-7WZK>].

⁵ Gen Z and Millennials account for over two thirds of the shopping on Afterpay’s platform. Since 2020, Afterpay’s consumer spending by Gen Z increased by more than 260% and Millennials increased by more than 180%. Felicity Robinson, *Inside the Latest Afterpay Report on Consumer Trends*, AFTERPAY (Sep. 2021), <https://www.afterpay.com/en-US/for-retailers/access/news/next-gen-index-us-september-2021> [<https://perma.cc/Y6EE-P6PB>].

⁶ Millennials are typically categorized as consumers born between 1981 to 1996 and Generation Z consists of consumers born between 1997 to 2012. *Disrupting The \$8T Payment Card Business: The Outlook On ‘Buy Now, Pay Later’*, CB INSIGHTS (Mar. 2, 2021), <https://www.cbinsights.com/research/report/buy-now-pay-later-outlook/> [<https://perma.cc/JQ59-7NVC>].

⁷ “Millemmas are when the everyday hurdles of older generations are experienced by a person from the millennial generation.” Nick Molnar, *The Millemma of the Millennial Legacy (and Why We Need to Smash the Millennial Stereotypes)*, LINKEDIN (Sep. 6, 2017), <https://www.linkedin.com/pulse/millemma-millennial-legacy-why-we-need-smash-nick-molnar/> [<https://perma.cc/YU97-2ZP4>].

⁸ Janice Gassam Asare, *Dear Businesses: Generation Z Does Not Want To Hear “Please Hold.”* FORBES (Nov. 11, 2019), <https://www.forbes.com/sites/janicegassam/2019/11/11/dear-businesses-generation-z-does-not-want-to-hear-please-hold/?sh=55b6733e6b46> [<https://perma.cc/Z97F-LME8>].

⁹ As compared to a direct or hard check, a soft check on a consumer’s credit score does not affect the consumer’s credit score. Typically, when consumers are applying for traditional credit cards, the creditors do a “hard pull,” which may negatively impact a consumer’s credit score because it indicates the frequency at which the borrower is seeking additional credit. Julia Kagan, *Soft Credit Check*, INVESTOPEdia (Mar. 24, 2021), <https://www.investopedia.com/terms/s/soft-inquiry.asp> [<https://perma.cc/W54C-NFFE>].

offerings to young consumers.¹⁰ Although well-intended and altruistic in purpose,¹¹ these highly protective amendments inadvertently hassled a whole generation of credit. First, the Act mandated consumers under the age of twenty-one to either have a parent cosigner or show sufficient proof of income.¹² Moreover, the CARD Act prohibited credit bureaus, such as Equifax, Experian, and Transunion, from sharing credit information of consumers under the age of 21 to potential lenders and consumer banks, like Mastercard and Chase Bank respectively.¹³ This prohibition made it far less likely for young adults to receive prescreened credit card offers.¹⁴ Lastly, it added a unique protection for college students¹⁵ by prohibiting universities and credit card providers from offering tangible inducements like t-shirts and required higher levels of disclosure from both the universities and credit card issuers.¹⁶

Together, these provisions limited Millennials' and continue to limit Gen Z's access to credit products at younger ages, which has and is preventing these consumers from accumulating longer, healthier credit histories. A low credit score may make it more difficult to borrow, and even if the consumer qualifies for the credit product, the consumer will most likely have to pay a higher interest rate to account for their greater default risk.¹⁷ In 2020, with credit scores hindered from the lack of credit history, a third of Millennials were rejected for credit products.¹⁸ Due to the under-supply of credit from traditional lenders to consumers, Afterpay, Affirm, and other marketplace lenders bypass consumer-protective regulatory practices by extending credit to an otherwise disqualified group of consumers.

Given the perceived exploitation of young consumers along with the recent surge in these new financial products' popularity, consumer advocates are now calling for deeper regulatory scrutiny of BNPL loans. In this article, I will explore how federal and state governments can

¹⁰ 15 U.S.C. § 1637 (2009); see 155 CONG. REC. 12,284 (2009) (statement of Sen. Menendez) (Comparing prescreened credit card offers to the subprime loans, and asserting that “[w]e cannot allow the credit card problem to become the next foreclosure crisis”); *Id.* at 12,283 (statement of Sen. Menendez) (“[W]e see gathering clouds in this economic storm and those clouds are credit card debt.”); *Id.* at 12,085 (statement of Sen. Dodd) (comparing the lending practices of credit card companies that do not verify ability to repay to those of lenders that caused the mortgage crisis).

¹¹ Studies show that students had both significantly higher numbers of cards and higher outstanding balances at schools that allowed on-campus solicitation. Phylis M. Mansfield & Mary Beth, *Marketing Credit Cards to College Students: Will Legislation Protect Them From Excessive Debt?*, 17 MKTG. MGMT. J. 1, (2007).

¹² 15 U.S.C. § 1637(e) (2009).

¹³ 15 U.S.C. § 1681(c)(1)(B) (2009).

¹⁴ *Id.*

¹⁵ ‘College student’ means an individual who is a full-time or a part-time student attending an institution of higher education. 15 U.S.C. § 1637(r)(1)(C) (2009).

¹⁶ 15 U.S.C. § 1637(r) (2009).

¹⁷ Daniel Kurt, *The Side Effects of Bad Credit*, INVESTOPEDIA (June 11, 2021),

<https://www.investopedia.com/the-side-effects-of-bad-credit-4769783> [<https://perma.cc/7TCZ-4FZH>].

¹⁸ Bankrate commissioned YouGov Plc to conduct the poll. All figures, unless otherwise stated, are from YouGov. Total sample size was 3,780 adults. Fieldwork was undertaken between Oct. 21-26, 2020. The survey was carried out online. Allie Johnson, Denied: Many Americans Have Been Turned Down for Credit in 2020, BANKRATE (Nov. 23, 2020), <https://www.bankrate.com/finance/credit-cards/credit-denial-survey/#methodology> [<https://perma.cc/E8TM-835M>].

regulate novel financial services to provide higher consumer protection while accommodating market demand. Part II discusses the economic structure of BNPL arrangements and the rationales for developing BNPL arrangements. Part III considers the federal and state regulation applicable to BNPL arrangements. Part IV analyzes consumer protection issues based on improper disclosure of negative credit impact and hidden fees associated with the use of the product, and calls for a more comprehensive approach to applicable legislation and subsequent regulatory enforcement of BNPL lenders’ violations of basic consumer rights. Part V proposes how consumer credit regulation in America should be incrementally reformed with respect to BNPL credit.

II. THE “BNPL” BUSINESS MODEL ANALYSIS

This Part describes how BNPL lending works. As distilled into its simplest form, a BNPL is a “cost-free” agreement that allows a consumer to receive her purchase and pay off the value of the item, over time.

Before delving into the discussion on the business rationale of BNPL lending, first, consider a hypothetical young consumer. She is a twenty-six-year-old woman who works as a full-time waitress at a nearby restaurant. About a month ago, intrigued by the idea of not having to pay for things right away, she made a \$200 purchase on a BNPL platform, which immediately extended to her a credit allowance of \$600. At the time, she opted in for the automated payment service because she is forgetful and didn’t want to incur a late fee. But much to her chagrin, her current monthly bank statement shows a \$35 nonsufficient fund (NSF) fee on her first debit card, a \$25 overdraft on her second debit card, and a BNPL late fee of \$7. Alarmed, she decides to use her money allocated for essential living expenses to fully pay off the remaining BNPL installments.

A. THE BUSINESS MODEL OF BNPL LOANS

The BNPL business model primarily focuses on financing lower cost items, usually less than \$250, which are paid back in installments every two weeks or full repayment after a few weeks.¹⁹ BNPL is a payment platform that creates an installment agreement²⁰ among the consumer, the merchant, and the third-party lender. In practice, the consumer purchases goods and services from the merchant by paying only a fraction of the purchase value at the time of sale.²¹ The third-party lender pays the full

¹⁹ Puneet Dikshit, Diana Goldstein, Blazej Karwowski, Udai Kaura & Felicia Tan, *Buy Now, Pay Later: Five Business Models to Compete*, MCKINSEY & CO. (July 29, 2021), <https://www.mckinsey.com/industries/financial-services/our-insights/buy-now-pay-later-five-business-models-to-compete> [https://perma.cc/474J-6U6D].

²⁰ Installment loans are a way to borrow money for a single purchase, such as a car or a house. Typically, the borrower receives the lump sum and pays down the debt over time, in installments. This is different than the typical credit card because instead of continuously borrowing money, installment loans are closed once fully repaid. Emily Gerson, *What is An Installment Loan?*, FORBES: ADVISOR (Apr. 17, 2020), <https://www.forbes.com/advisor/loans/what-is-an-installment-loan/> [https://perma.cc/W687-D29H].

²¹ This is also often known as a point of sale (POS) financing which is a convenient lending option that lets consumers make purchases with incremental payments. *Id.*

purchase value less any merchant fees to the merchant.²² Then, the consumer maintains a relationship with the third-party lender and pays off the balance in a series of four, zero-interest installments.²³

Considering the nature of these “cost-free” loans, BNPL lenders do not derive their revenues from the traditional interest payments. Instead, BNPL lenders mainly rely on merchant network revenue (including affiliate fees) and consumer late penalties.²⁴ For the purposes of this analysis, this section is going to focus on two BNPL providers, Afterpay and Affirm.

B. Merchant Network Fees

Merchant network fees are one of the largest revenue drivers for BNPL service providers. In 2021, Affirm generated \$350 million and Afterpay generated \$137 million of their revenues from merchants alone.²⁵ Generally, merchant network fees vary based on the agreement and terms of the product offering, which are largely comprised of regular transactions and affiliated marketing. The transactional fee²⁶ is collected from merchants for each transaction determined as a percentage of the value of the goods purchased by the consumer. For example, the consumer will buy the product for the full price of \$100, but the merchant will take a discount and receive only \$96 from the third-party lender. Upon the consumer’s repayment, the lender will generate a profit of \$4. In effect, this would mean that the lender would profit \$4 from the total exposure of \$71 over the lifetime of the loan. It is \$71 because typically, the first payment is due at the time of purchase. Therefore, the lenders only carry the risk of the remaining payments. If we repeat this transaction four times over, the lender has profited \$16 from loans which have an average balance of \$71 over the duration of its lifetime. In addition, revenue from affiliated marketing is generated when consumers make a purchase on a

²² Sellers or merchants are often charged a fee for accepting BNPL payments, but are still willing to provide this type of payment method if they believe that it will generate more sales or keep them competitive in the market. Chay Fisher, Cara Holland & Tim West, *Developments in the Buy Now, Pay Later Market*, RSRV. BANK OF AUSTRALIA BULL. (March, 2021), <https://www.rba.gov.au/publications/bulletin/2021/mar/pdf/developments-in-the-buy-now-pay-later-market.pdf> [https://perma.cc/U6NS-L4Y2].

²³ *Id.*

²⁴ Sasha Hupka, *Buy-Now-Pay-Later Apps: How They Work*, L.A. TIMES (Aug. 11, 2021, 5:00 A.M.), <https://www.latimes.com/politics/story/2021-08-11/buy-now-pay-later-apps-how-they-work> [https://perma.cc/G3RT-5363].

²⁵ Affirm Holdings, Inc., *Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the Fiscal Year Ended June 30, 2021*, AFFIRM (June 30, 2021), <https://investors.affirm.com/static-files/b85853cf-b293-46f8-a6e9-e63c0287e6f1> [https://perma.cc/6TMD-LVLG] [hereinafter “SEC filings, Affirm”]; Afterpay, *Afterpay Limited FY21 Annual Report* (Aug. 25, 2021), <https://afterpay-corporate.yourcreative.com.au/wp-content/uploads/2021/08/APT-FY21-Annual-Report.pdf> [https://perma.cc/UX43-46KN] [hereinafter “Limited Annual Report, Afterpay”].

²⁶ Karen Kwok & Peter Larsen, *Breakdown: Buy Now, Pay Later’s Bill is Coming Due*, REUTERS (Oct. 14, 2021, 2:16 A.M.), <https://www.reuters.com/breakingviews/breakdown-buy-now-pay-laters-bill-is-coming-due-2021-10-14/> [https://perma.cc/B777-GS87].

merchant’s website after being directed from an advertisement on Affirm or Afterpay’s website or mobile application.

C. Late Fees

Finally, although BNPL lenders advertise their loans as cost-free, some lenders include late fees, much like in the case of our hypothetical consumer.²⁷ Some BNPL lenders’ contracts charge a late fee of \$7 to customers and contain other provisions for additional fines in the future.²⁸ Further, the purchase price must be paid within the scheduled four payment periods and no extensions are permitted on each scheduled period.²⁹ For instance, if a consumer starts to consecutively miss their payments after their first payment until the end of the loan period, then the consumer would be charged with not only the initial \$10 late fee, but an additional \$7 late fee if the payment remains unpaid for an additional seven days after the due date. Consequently, in an instance where a consumer misses all four payments (\$17 late payment multiplied by 4 missed payments) and incurs the highest penalty of \$68 on a \$272 purchase, this would be approximately equivalent to a 25% monthly interest rate or an annual rate of 300%.³⁰ Comparatively, as of 2019, the national average interest rate for personal loans is 17% per year.³¹ Due to these practices, in 2021, Afterpay earned approximately \$87.3 million in revenue from late fees alone, with one-in-three of its consumers missing a payment.³² Analysts forecast that BNPL revenue generated from late fees will increase to \$340 million by 2023.³³

D. Beyond Revenue

Revenue alone, does not paint the full picture of BNPL’s operations. In fact, in 2021, Affirm and Afterpay reported significant losses, \$423 million and \$159 million, respectively.³⁴ The lenders incur three main costs of sales which include provision for credit loss, other transactional costs, and funding costs.³⁵ First, credit loss is the loss to the lender if a consumer fails to repay the full purchase price. In 2021, Affirm reported nearly \$246 million worth of losses on loan purchase commitment and Afterpay reported nearly \$194 million worth of

²⁷ Affirm does not charge late or missed payment fees, but Affirm does participate in soft credit checks before extending credits to consumers. *Id.*

²⁸ For American users, late fees are capped at 25% of the purchase price. In addition to the late fees, Afterpay reserves the right to charge an extra \$7 for every additional 7 late days. Moreover, if Afterpay is unable to collect the debt, then they will hand over the debt to a debt collector and charge an extrajudicial collection fee. AFTERPAY, *Installment Agreement - USA* (Aug. 2022), <https://www.afterpay.com/en-US/installment-agreement> [<https://perma.cc/JSU8-S4X4>].

²⁹ *See id.*

³⁰ Tony Boyd, *Afterpay’s Late Fees Anomaly*, FIN. REV.: CHANTICLEER (June 11, 2021, 12:00 A.M.), <https://www.afr.com/chanticleer/afterpay-s-late-fees-anomaly-20210610-p57zy0> [<https://perma.cc/PEC5-R39N>].

³¹ Brianna McGurran, *What’s a Good Personal Loan Interest Rate?*, EXPERIAN (Jan. 27, 2020), <https://www.experian.com/blogs/ask-experian/whats-a-good-interest-rate-for-a-personal-loan/> [<https://perma.cc/69CJ-BZ22>].

³² Limited Annual Report, Afterpay, *supra* note 25.

³³ *See id.*

³⁴ SEC filings, Affirm; Afterpay, Limited Annual Report, *supra* note 25.

³⁵ *See id.*

“receivable impairment,” a 106% increase from the prior year.³⁶ Second, BNPL lenders must pay transactional fees to other third-party payment infrastructures, such as the interchange fees, network fees, and issuer processors, because most of these platforms are merely “middle-men” with no access to consumers’ bank accounts.³⁷ Lastly, BNPL lenders’ most important cost is arguably finance cost, which is the lenders’ cost of capital to finance the gap between the time of when the payment is released to the merchants and when the consumers pay off the purchase.³⁸ Typically, these “middle-men” lenders borrow from bigger lenders, such as Goldman Sachs and Citibank that charge a negotiated annual interest rate on these types of loan facilities (usually payable on a monthly basis).

With astronomical losses, Afterpay reported a net profit margin of just 2.1%, which raises the question: Why is the market in a frenzy to offer BNPL services?³⁹ There are two plausible explanations. First, Credit Suisse projects that by 2024, BNPL payments will constitute 10% of all e-commerce transactions.⁴⁰ Additionally, Accenture finds that BNPL transactions already make up 6.5% of all fashion e-commerce in the U.S.⁴¹ Based on these two studies, market analysts project to see positive operating margins by 2023-2024.⁴² Second, other analysts speculate that many BNPL lenders intend to provide other financial services and to cross-sell other more profitable products by leveraging their wide consumer base. Given Affirm and Amazon’s recent partnership⁴³ that offers both traditional credit card products and BNPL services, the second explanation is more plausible. In 2021, only second to its merchant network fees, Affirm derived nearly 37% (\$326 million) of its revenue from interest fees

³⁶ This meteoric rise in principal payments that cannot be collected is alarming. See *supra* note 21.

³⁷ Non-banks are service providers, which range from small fintech start-ups to larger corporations, that offer payment-related services to consumers, but does not have bank, thrift, or credit union charter and does not take deposits. Marc Labonte, *Who Regulates Whom? An Overview of the U.S. Financial Regulatory Framework*, U.S. CONGRESSIONAL RESEARCH SERVICE, (RL344918; Mar. 10, 2020).

³⁸ *Buy Now Pay Later Headwinds Intensify Amid Rising Competition, Economic Uncertainty (Profits, Growth May be Further Pressured by Rising Credit and Funding Costs)*, FITCH RATINGS (July 28, 2022), <https://www.fitchratings.com/research/non-bank-financial-institutions/buy-now-pay-later-headwinds-intensify-amid-rising-competition-economic-uncertainty-profits-growth-may-be-further-pressured-by-rising-credit-funding-costs-28-07-2022> [<https://perma.cc/L57R-ZU7D>].

³⁹ Zijia Song, *BNPL Seen as Growing Competitor to Debit Cards*, BLOOMBERG (Sept. 20, 2021), <https://www.bloomberg.com/news/articles/2021-09-20/buy-now-pay-later-seen-as-growing-competitor-to-debit-cards> [<https://perma.cc/FBL8-6279>].

⁴⁰ Timothy Chiodo, Nik Cremona, Justin Forsythe, and Moshe Orenbuch, *Payments, Processors, & Fintechs (If Software Is Eating the World.... Payments Is Taking a Bite)*, CREDIT SUISSE EQUITY RESEARCH | AMERICAS (2020), https://research-doc.credit-suisse.com/docView?language=ENG&format=PDF&sourceid=csplusresearchcp&document_id=1082106811&serialid=91taQaLeKMYkTfzB0rHonfefWNL6W5uABHoXHk5EVRA%3D [<https://perma.cc/3GWF-GGJ2>].

⁴¹ Imran Amed et al., *The State of Fashion*, MCKINSEY & COMPANY (2020), <https://www.mckinsey.com/industries/retail/our-insights/state-of-fashion> [<https://perma.cc/7VG7-6ZMZ>].

⁴² *Supra* note 39.

⁴³ Alex Lazarow, *Amazon & Affirm’s BNPL Deal, And Three Predictions About What It Means For Fintech*, FORBES (Aug. 30, 2021), <https://www.forbes.com/sites/alexlarazow/2021/08/30/amazon--affirms-bnpl-deal-and-three-predictions-about-what-it-means-for-fintech/?sh=6c2db82e6b5a> [<https://perma.cc/F4J6-G4QB>].

ranging from 1% to 30% on its traditional credit product offerings.⁴⁴ Regardless of future product offerings, BNPL is here to stay, so it is important to understand the applicable regulators and regulations.

II. THE APPLICABLE FEDERAL AND STATE LAWS THAT BNPL LENDERS SEEK TO AVOID

Laws and regulations that apply to the current BNPL lending practices are governed by both federal (the U.S. Federal Trade Commission (FTC) and the Consumer Finance Protection Bureau (CFPB)) and state (Attorney General Offices and Consumer Affairs Departments) agencies.

Generally, BNPL loans resemble traditional retail installment loans or credit sales. Still, BNPL differs from these loans in small but significant ways. These differences allow BNPL lenders to be treated by regulators as payment platform providers, who coordinate and facilitate installment payments on behalf of consumers, rather than as creditors. However, due to the prevalent imbalance of power in lender-borrower relationships,⁴⁵ there is an urgent need to provide more clarity around the applicability of laws granting protection to this novel method of consumer borrowing.

A. Applicable Federal Agencies

Of the many federal laws, regulations, and agencies that protect consumers in the financial marketplace, two agencies may impose the greatest supervisory check on BNPL lenders: the FTC and the CFPB.⁴⁶ Under Section 5 of the Federal Trade Commission Act (FTCA), the FTC has enforcement authority against nonbank lenders practicing any unfair or deceptive practice or act (UDAP) affecting commerce.⁴⁷ Similarly, as created under the Dodd-Frank Act (Dodd-Frank), the CFPB can “supervise a nonbank covered person when the Bureau has reasonable cause to determine, by order. . . that such person is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.”⁴⁸ Given the aligned purpose of both agencies, the regulators often share joint jurisdictions of nonbank entities.⁴⁹ Despite their overlapping authorities, the CFPB is better suited to use its authority to supervise and enforce compliance with federal law, including the Truth in Lending Act (TILA)

⁴⁴ SEC Filings, Affirm, *supra* note 23.

⁴⁵ “Dishonest and greedy lenders can and do take advantage of the legal loopholes to the detriment of honest lenders and borrowers alike.” Elizabeth Renuart & Diane E. Thompson, *The Truth, The Whole Truth, and Nothing but the Truth: Fulfilling the Promise of Truth-in-Lending*, 25 YALE J. REG. 181, 207 (2008).

⁴⁶ Kwesi D. Atta-Krah, *Preventing a Boom from Turning Bust: Regulators Should Turn Their Attention to Starter Interrupt Devices before the Subprime Auto Lending Bubble Bursts*, 101 IOWA L. REV. 1187, 1199 (2016).

⁴⁷ 15 U.S.C. § 45(a)(1).

⁴⁸ CFPB, *Procedural Rule to Establish Supervisory Authority over Certain Nonbank Covered Persons Based on Risk Determination*, Docket No.: CFPB-2012-0021, https://files.consumerfinance.gov/f/201206_cfpb_final-rule_certain-nonbank-covered-persons-risk-determination.pdf.

⁴⁹ In 2019, the CFPB and the FTC renewed their Memorandum of Understanding (MOU) that recognizes that effective cooperation between the two groups is critical for the equitable protection of all consumers, prevents duplication of efforts, provides consistency, and ensures a vibrant marketplace for consumer financial services. *Memorandum of Understanding Between the CFPB and the FTC* (2019).

and provisions banning unfair, deceptive, and abusive acts and practices. The agency is also best situated to obtain information about the BNPL risks posed to consumers because the CFPB was created for this very purpose—regulatory accountability.⁵⁰

1. Unfair, Deceptive, or Abusive Acts or Practices

Prior to Dodd-Frank, the FTC protected consumers through the prohibition on unfair and deceptive acts and practices under the FTCA, as well as through the provisions and requirements in TILA. Dodd-Frank not only created the CFPB, but also added to those prohibitions the first federal provisions on “abusive” acts or practices. These added provisions not only overlap existing prohibitions but go beyond what has been prohibited as UDAPs. Unfair, Deceptive, or Abusive Acts or Practices (UDAAP) are business behaviors that can “cause significant financial injury to consumers, erode consumer confidence, and undermine the financial marketplace.”⁵¹ Or, as they are more commonly described, acts that one would not wish upon their grandmothers.⁵²

Given this rather broad regulatory approach, UDAAPs have been largely defined through agency enforcement, resulting in orders or settlement agreements.⁵³ Arguably, the statutory language banning UDAAPs is intentionally broad because a transaction that is in technical compliance with other federal and state law can still constitute a UDAAP.⁵⁴ When an entity is found in violation of UDAAP, it can lead to large fines and civil lawsuits, as well as significant damage to the company’s reputation.⁵⁵

⁵⁰ “Because consumer protection was everyone’s responsibility, it became no one’s responsibility.” Only the FTC had consumer protection as its primary role, but even at best, it had a very restricted scope with regards to financial services. Therein, to strengthen broad regulatory accountability, the CFPB was created. See Adam J. Levitin, *The Consumer Financial Protection Bureau: An Introduction*, 32 REV. BANKING & FIN. L. 321, 330, 334-339 (2013).

⁵¹ See generally CONSUMER FIN. PROT. BUREAU, CFPB Supervision and Examination Manual, Procedures 1 (Oct. 2012), https://files.consumerfinance.gov/f/201210_cfpb_supervision-and-examination-manual-v2.pdf#semanal [<https://perma.cc/EJ33-YJXE>] (providing standards used to evaluate UDAAPs in different contexts).

⁵² The standard for unfairness is when: (1) it causes or is likely to cause substantial injury to consumers; (2) the injury is not reasonably avoidable by consumers; and (3) the injury is not outweighed by countervailing benefits to consumers or to competition. A representation, omission, act, or practice is deceptive when (1) the representation misleads or is likely to mislead the consumer; (2) the consumer’s interpretation of the representation is reasonable under the circumstances; and (3) the misleading representation is material. An abusive practice materially interferes with the ability of the consumer to understand a term or condition of the financial product or takes unreasonable advantage of the consumer’s lack of understanding, inability of the consumer to protect her interest or when there was reasonable reliance by the consumer on a covered person to act in the interests of consumer. See 12 U.S.C. § 5481, 5531 & 5536(a).

⁵³ See *supra* note 50.

⁵⁴ Every examiner of consumer complaints should take into consideration the context and reliability of each complaint and a consumer complaint does not have to be indicative of a violation of law. However, when there are repeated complaints lodged against an institution, this may warrant further review or flagging of the issue. See *supra* note 50.

⁵⁵ Jim Letton, *What is UDAAP? Avoiding Unfair, Deceptive, Abusive Acts or Practices by Complying with Federal Law*, JDSUPRA (July 22, 2021), <https://www.jdsupra.com/legalnews/what-is-udaap-avoiding-unfair-deceptive-8341996/>.

2. The Consumer Financial Protection Act, The Equal Credit Opportunity Act, Fair Credit Reporting Act, The Fair Debt Collection Practices Act, and The Truth in Lending Act

There are a multitude of federal consumer protection laws applicable to BNPL lenders, but these lenders manage to skirt one of the most important federal disclosure laws by evading the definition of “creditor” and “credit.” Credit is “the provision of money, goods, or services with the expectation of future payment.”⁵⁶ As intuitive as credit can be for most consumers, the federal credit consumer laws often contain varying technical interpretations of credit.

The Consumer Financial Protection Act of 2010 (CFPA) defines “credit” as the “right granted by a person to a consumer to defer payment of a debt, incur debt and defer its payment, or purchase property or services and defer payment for such purchase.”⁵⁷ Similar definitions of “credit” appear in the Equal Credit Opportunity Act (ECOA)⁵⁸ and the Fair Credit Reporting Act (FCRA),⁵⁹ which references the ECOA’s definition.⁶⁰ The ECOA and FCRA define a creditor as “any person who regularly extends, renews, or continues credit.”⁶¹ Additionally, the Fair Debt Collection Practices Act (FDCPA),⁶² which governs debt collection activities, defines “creditor” as “any person who offers or extends credit, or to whom a debt is owed.”⁶³ The language of these statutes covers BNPL loans as “credit” because installment payments are forms of deferred payments. Further, as defined by the prior statutes, BNPL lenders are “creditors” because they offer debt that is owed by consumers. Thus, when BNPL platforms are found in violation of any of these provisions, these statutes can be enforced.

Similarly, TILA is an important federal consumer protection law because this disclosure regulation requires all “covered” credit providers to disclose the fees and charges; the annual percentage rate (APR), the due dates of all the scheduled payments; and, the amount of any late payment charges.⁶⁴ However, TILA defines a “creditor” as:

A person who both regularly extends. . . consumer credit which is payable by an agreement in more than four

⁵⁶ *Credit*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/credit>, (Nov. 11, 2021).

⁵⁷ Debt is not defined. 12 U.S.C. § 5481(7).

⁵⁸ The ECOA makes it unlawful for any creditor to discriminate against any applicant on the basis of race, color, religion, national origin, sex, marital status, or age. 15 U.S.C. § 1691.

⁵⁹ The FCRA promotes accuracy, fairness, and privacy of consumer information as applied to consumer reporting agencies. 15 U.S.C. § 1681.

⁶⁰ Equal Credit Opportunity Act (ECOA), 15 U.S.C. § 1691a(d); Fair Credit Reporting Act (FCRA), 15 U.S.C. § 1681a(r)(5).

⁶¹ *Id.*

⁶² A debt collector may not use unfair or unconscionable means to collect or attempt to collect any debt. For example, a debt collector may not call before 8 a.m. or after 9 p.m., call consumers at work, employ unfair practices in to collect debt, or conceal his identity on the phone. 12 CFR § 1006.22 (2021).

⁶³ 15 U.S.C. § 1692(a)(4).

⁶⁴ Truth-in-Lending Act (TILA), Pub. L. No. 90-321, 82 Stat. 146 (1968) (current version at 15 U.S.C. § 1601 (2018)).

installments⁶⁵ or for which a payment of a finance charge is or may be required and the debt arising from the consumer credit transaction is initially payable on the face of the evidence of indebtedness.⁶⁶

As applied, BNPL lenders are not “creditors” under TILA because BNPL lenders do not impose a finance charge, such as an interest rate or service fee, and all loans made are contracted to be paid in an installment of exactly four or less payments. Some consumer advocates may argue that TILA disclosures apply to BNPL loan transactions because late fees can be construed as a finance charge. However, a CFPB rule excludes late payment charges from finance charges when the late fees are sanctioned for “failure to make payments as agreed.”⁶⁷ Consequently, there is a strong argument that BNPL lenders are not subject to TILA loan disclosure rules.

B. Applicable State Agencies

As demonstrated above, the lenders of these novel financial services exploit the gaps in the federal regulatory system to avoid basic consumer protections. Fortunately, state regulators and lawmakers, such as each state’s respective Attorney General’s office and Consumer Affairs office, can step in to fill in the federal blind spots. As part of Dodd-Frank, “state consumer finance law”⁶⁸ is preempted only if it “prevents or significantly interferes with” the exercise of banking powers authorized under federal law.⁶⁹ Effectively, Dodd-Frank created a federal floor for consumer protection by stating that “a statute, regulation, order, or interpretation in effect in any State is not inconsistent with the provisions of this title if the protection that such statute, regulation, order, or interpretation affords to consumers is *greater* than the protection provided under this title.”⁷⁰

Currently, there are two state consumer protections that can be broadly applied to BNPL lenders: regulatory enforcement through an individual state’s Retail Installment Acts and state supervisory authority through licensures. To this end, some states cannot enforce their installment acts for the same reasons that the CFPB and FTC cannot

⁶⁵ In a Federal Reserve Board Letter of March 3, 1970, the Board stated that it felt that it was imperative to make transactions involving more than four installments subject to the Act’s requirements, “since without this provision the practice of burying the finance charge in the cash price . . . would have been encouraged.” Federal Reserve Board Letter by J.L. Robertson, March 3, 1970, in 4 CCH Consumer Credit Guide II 30, 320, at 66,147 (1970).

⁶⁶ 15 U.S.C. § 1602a(g).

⁶⁷ 12 C.F.R. § 1026.4(c)(2)(1)(ii).

⁶⁸ As defined, a state consumer law is a state law that does not directly or indirectly discriminate against national banks and that directly and specifically regulates the manner, content, or terms and conditions of any financial transaction (as may be authorized for national banks to engage in), or any account related thereto, with respect to a consumer. 12 U.S.C. § 25b(a)(2).

⁶⁹ 12 U.S.C. § 25b(b).

⁷⁰ 12 U.S.C. § 5551(a)(2).

enforce TILA. States have been strengthening their supervisory and enforcement authorities through licensing.

1. State Retail Installment Loan Acts

Due to the prevalent nature of retail installment loans, each state has enacted robust statutory language concerning the definition of installment credit and establishing regulatory requirements and penalties for violations. Two of the most comprehensive state statutory schemes can be found in New Mexico’s Retail Installment Sales Act and the Illinois Retail Installment Sales Act. Under both Acts, a retail installment transaction means any transaction that the buyer agrees to pay the unpaid balance “in one or more installments”⁷¹ and any applicable creditor engaging in such transaction must comply with either the state’s disclosure requirements or with TILA.⁷²

Along with disclosure requirements, the Acts only allow the holder of the retail installment contract to collect a late charge not exceeding 5% of each payment or \$5, whichever is less.⁷³ Any larger late fee will violate the statute. However, despite its robust language, the penalty is relatively weak because the lender is only required to refund the collection of late charges or price differential fees and is fined a civil penalty of no more than \$1,000.⁷⁴ The lender may still recover their principal loan.⁷⁵ Therein, bringing BNPL lenders under this provision’s enforcement would seemingly be ineffective because noncompliance with the statute does not render the loans uncollectible.

Some states that grant greater penalties exclude BNPL lenders. Arizona’s Retail Installment Act, California’s Retail Installment Act (known as the Unruh Act), Colorado’s Consumer Credit Code, and Massachusetts’s Retail Installment Sales and Services carve out installment transactions as either: (a) payables of *more than four* installments (excluding a finance charge for the state of Colorado and Massachusetts);⁷⁶ or (b) including a finance charge.⁷⁷

For the same reasons that BNPL lenders escape TILA, those lenders are exempted under these state laws. The lenders’ regulatory arbitrage deprives consumers of their most basic protections because in California, Colorado, and Massachusetts, if the retail seller and retail buyer engage in a retail installment transaction covered by those states’ laws, then the retail seller must be in compliance with the federal TILA provisions or provide the retail buyer with the necessary terms such as

⁷¹ N.M. Stat. Ann. § 56-1-1(G) (2011); 815 ILCS § 405-2.5 (1998).

⁷² The state disclosure requirement is highly comprehensive and the creditor must provide: the cash sale price, the down payment, the aggregate amount less fees, the principal balance, the maximum number of installment payments, the due date of each payment, the amount of the time price differential and the amount of the time balance owed by the buyer to the seller. See N.M. Stat § 56-1-2 (2006); 815 ILCS § 405-5 (1998).

⁷³ See N.M. Stat. § 56-1-15 (2006); for the state of Illinois, the late charge is 5% of each payment or \$10, whichever is less. 815 ILCS § 405-12 (1998).

⁷⁴ N.M. Stat § 56-1-8 (2006); 815 ILCS § 405-31 (2006). See Civil Penalties, N.M. Stat § 56-1-12(K); 815 ILCS § 405-2.16.

⁷⁵ *Id.*

⁷⁶ Co. Rev. Stat. § 5-1-301(32) (2016); A retail installment agreement is either (a) a transaction with one or more payments and a finance charge or (b) a transaction with five or more payment without a finance charge. Mass. Gen. Laws Ch. 255D, § 1 (2006).

⁷⁷ Ariz. Rev. Stat. § 44-6001(2012); C.A. Civ. Code § 1802.6 (1959); *Id.* Rev. Stat. § 28-41-301(2016).

interest rate, loan size, and other disclosures.⁷⁸ In some states, noncompliance with these disclosures could mean that the lenders are barred from recovery of the undisclosed fees⁷⁹ or incur heavy penalties.⁸⁰

As seen above, some of the states with the most substantive disclosure provisions and heaviest violation penalties exclude BNPL lenders. However, some states separately require TILA or similar types of disclosures through state licensing requirements.

2. State Licensing Requirements

Licensing, or “gatekeeping” authority, is fundamental to state supervision. It is usually a prerequisite for nonbanks to conduct business in a given state.⁸¹ In most cases, absent a state license, a nonbank cannot conduct any business activity with consumers in that state.⁸² Typically, this allows each state to investigate and examine consumer risks and to provide administrative, civil, and criminal remedies to consumers who were harmed by the licensees.⁸³

The “installment lender” or “small loan” license is currently required in California,⁸⁴ Louisiana,⁸⁵ Maryland,⁸⁶ Missouri,⁸⁷ North Dakota,⁸⁸ New Mexico,⁸⁹ Rhode Island,⁹⁰ South Dakota,⁹¹ Washington,⁹²

⁷⁸ Section (b) states that every contract subject to this chapter shall contain disclosures required by Regulation Z whether or not Regulation Z applies to the transaction. C.A. Civ. Code §1803.3 (2019); Material disclosure requires the disclosure of annual percentage rate, the method of determining the finance charge, the amount of finance charge, the total payments, the number and amount of payment and the due dates and periods of repayment. Co. Rev. Stat. § 5-1-301(27) (2016); A transaction subject to the provisions of this chapter (“Truth-in-Lending Act”) is also subject to the consumer credit cost disclosure. Mass. Gen. Laws Ch. 255D § 31 (2006); Mass. Gen. Laws Ch. 140D (2006).

⁷⁹ C.A. Civ. Code § 1812.7 (1970); Ariz. Rev. Stat. § 44-6006 (2012); Mass. Gen. Laws Ch. 140D, § 33(c).

⁸⁰ Co. Rev. Stat. § 5-5-201 (2016).

⁸¹ Conf. of State Bank Supervisors, *Reengineering Nonbank Supervision Chapter Two: Overview of Nonbank Supervision*, CONF. OF STATE BANK SUPERVISORS, (2019),

https://www.csbs.org/sites/default/files/chapter_two_-_overview_of_state_nonbank_supervision_2.pdf

[<https://perma.cc/YT5E-45M8>].

⁸² *Id.*

⁸³ *Supra* note 79.

⁸⁴ Cal. Fin. Code § 22100 (2009).

⁸⁵ La. Rev. Stat. Ann. § 9:3561.1 (2010).

⁸⁶ The licensure is applicable to a loan of less than \$25,000 or less made for personal, family, or household purpose *regardless of whether the transaction is or purports to be an installment loan*. Md. Code Ann., Com. Law § 12-303(2).

⁸⁷ Mo. Rev. Stat. § 364.030 (2015).

⁸⁸ N.D. Cent. Code § 13-04.1-02 (2015).

⁸⁹ N.M. Stat. § 58-15-2 (2013).

⁹⁰ R.I. Gen. Law § 19-14-3 (2014).

⁹¹ S.D. Codified Laws § 54-4-36 (2011).

⁹² Wash. Rev. Code § 31.04.015 (2008).

Nevada,⁹³ Georgia,⁹⁴ Ohio,⁹⁵ Illinois,⁹⁶ and Hawaii.⁹⁷ Similar to the TILA provisions, in Hawaii, Georgia, Nevada, Illinois, South Dakota, North Dakota,⁹⁸ Maryland,⁹⁹ and Ohio, all licensed installment lenders to provide specific data to borrowers.¹⁰⁰ This data includes a copy of the loan contract with distinct terms, the date of the loan, the amount of the obligation, the date of its maturity, and the description or schedule of payments on that loan.¹⁰¹ In California, any willful violation of the state licensing provision renders the loan void and uncollectible,¹⁰² and in Rhode Island, any lenders who make an invalid loan under the licensing provision will have no right to collect any interest, fees, or charges.¹⁰³

Although BNPL lenders fall under the supervision of states’ licensing statutes, some states are still not protective of their consumers. For example, in Ohio, lenders can charge the greater of \$15 or 5% of the installment due,¹⁰⁴ which is more than most BNPL late fee charges. Furthermore, if the consumer’s bank account has insufficient funds, then lenders can charge up to \$20 plus the actual insufficient fee charge assessed by the consumer’s bank.¹⁰⁵ Similarly, Illinois allows lenders to charge \$25 plus the actual insufficient fee charge assessed by the consumer’s bank.¹⁰⁶

Currently, the most protective state licensing legislation, which went into effect on January 1, 2022, is in Hawaii. Not only must the licensee comply with TILA and the additional state disclosure regulation, such as the provision of electronic copies, but the lender is also prohibited from repeated payment withdrawals after the second failed attempt.¹⁰⁷ Lastly and most notably, Hawaii added a provision that is highly consumer-friendly, but typically extended to mortgage borrowers. That is,

⁹³ In Nevada, the licensing requirement is applicable to all lenders making installment loans unless they are otherwise subject to other regulations for high interest loan services or deferred deposit loan services. N.R.S. § 675.035 (2005).

⁹⁴ In 2020, the state of Georgia amended its Installment Loan Act to expand its substantive coverage to apply to any lender making any loan to an individual of \$3,000 or less, regardless of the interest rate. Prior to the amendment, the Act generally only applied to small loans less than \$3,000 with an interest rate of at least eight percent. By this expansion, all installment lenders who make loans below \$3,000 are subject to Georgia’s installment loan licensing obligations which require additional consumer protections such as loan term disclosures after the sale. Pursuant to the Georgia Installment Loan Act, an installment loan means an agreement to make a loan to an individual in an amount of \$3,000 or less, including the renewal or refinancing of any such loan. O.C.G.A § 7-3-4 (2010).

⁹⁵ In Ohio, any small loans that is \$5,000 is subject to lender licensing requirements. Ohio Rev. Code Ann. § 1321.02 (2008).

⁹⁶ Under Illinois’ Interest Act, any lenders making consumer loans under \$40,000 must be licensed. 815 Ill. Comp. Stat. Ann. § 205 (2002).

⁹⁷ H.B. 1192, https://www.capitol.hawaii.gov/session2021/bills/HB1192_CD1_.HTM.

This list may not include all states requiring licensing provisions.

⁹⁸ In all dealings between borrower and lender, the lender is charged with a duty to fully and fairly inform the prospective borrower of all liabilities, costs, and other financial obligations that can be or will be incurred by the borrower if the borrower uses the services of the lender. N.D. Admin. Code § 13-05-01-03.

⁹⁹ The lender compliance with the applicable disclosure provisions of TILA is sufficient to meet the requirements of this title. Md. Code Ann., Com. Law § 12-106(b).

¹⁰⁰ *Supra* note at 97.

¹⁰¹ O.C.G.A § 7-3-15 (2010); N.R.S. § 675.360 (2005); Ohio Rev. Code Ann. § 1321.67 (2008); Md. Code Ann., Com. Law § 12-308(a); S.D. Codified Laws § 54-4-58 (2011).

¹⁰² Cal. Fin. Code § 22750 (1994).

¹⁰³ R.I. Gen. Law § 19-14-26.1 (1995).

¹⁰⁴ Ohio Rev. Code Ann. § 1321.68(K) (2017).

¹⁰⁵ A licensee may charge a collection fee not greater than \$20 plus any amount passed on from the bank for instrument returned or dishonored for any reason. Ohio Rev. Code Ann. § 1321.68(J) (2017).

¹⁰⁶ 205 Ill. Comp. Stat. §670/11 (2002).

¹⁰⁷ *See supra* note 95.

the state allows borrowers to rescind their loans within three days by returning the principal and, upon which, the lender must return the originally signed agreement.¹⁰⁸

BNPL Exempted States

Yet again, like the earlier mentioned regulatory arbitrage, some states' licensure¹⁰⁹ requirements exempt BNPL lenders because of regulatory loopholes. For example, New Mexico requires licenses for all small loans less than \$5,000, but the statute only covers installment loans that must be repaid "in four substantially equal payments. . .with an initial stated maturity of not less than one hundred twenty days to maturity."¹¹⁰ Typically, most BNPL loans are due between six to eight weeks, which is approximately forty-two to fifty-six days.¹¹¹ This particular regulatory skirting of licensing is a significant evasion of consumer protection laws because under New Mexico's small loan licensing provisions, a licensee cannot attempt multiple withdrawals after the initial insufficient funds notice from the consumer's financial institution.¹¹² Moreover, it prohibits multiple delinquent charges on one late payment, which means that if New Mexico's licensing supervision applied, then a BNPL lender's current costly practice of the initial \$10 late fee in conjunction with an additional \$7 per seven days late on one missed payment would be prohibited.¹¹³ Washington prohibits late fees greater than 10% of the installment due and the lender can only charge an additional insufficient funds fee in an amount approved by the state.¹¹⁴ However, the state's licensure supervision only applies to loans that are lent with an interest or for a fee, which excludes BNPL loans from the state's consumer-friendly late fee requirements and in some cases, insufficient fee charges.¹¹⁵

On the other hand, some states licensing schemes that exempt BNPL lenders only provide weak protection. For instance, Louisiana's licensing requirement only applies to "consumer credit sales" in which a credit service is charged, and the purchaser is able to defer the payment in two or more installments.¹¹⁶ Hence, BNPL lenders are exempt because they do not charge a service fee when extending credit. Even if the state licensure applied, there are still no greater consumer protection rights. Louisiana permits not only a late charge fee of \$10 or 5% of the installment

¹⁰⁸ *Id.*

¹⁰⁹ Nebraska requires installment licenses, but restricts the definition of installment sale to just "transactions, in which a buyer acquires goods or services from a seller pursuant to an agreement which provides for a *time-price differential* and under which the buyer agrees to pay all or part of the time-sale price in one or more installments." Neb. Rev. Stat. Ann. § 45-335 (2013).

¹¹⁰ N.M. Stat. § 58-15-2 (2013).

¹¹¹ *Supra* note 3.

¹¹² N.M. Stat. § 58-15-20.1 (2013).

¹¹³ *Id.*

¹¹⁴ Wash. Rev. Code § 31.04.105(6) (2009).

¹¹⁵ Wash. Rev. Code § 31.04.015(14) (2009).

¹¹⁶ La. Rev. Stat. Ann. § 9:3516 (12) (2011).

due, whichever is greater, but also allows for the lender to assess an additional \$25 fee or 5% of the payment, whichever is greater, for insufficient funds in the consumer’s account.¹¹⁷ For consumers, this allows for far greater penalties than the ones already sanctioned by BNPL lenders.

A. State UDAP

Lastly, similar to the federal UDAAP, each state has its own model “UDAP” law. State mini-UDAP statutes vary in each of the fifty states. Further, all versions authorize enforcement by both the consumers and the state’s attorney general.¹¹⁸ This provision is particularly unique because it allows for private rights of action and provides consumers legal remedies for injuries stemming from deceptive and unfair business practices.¹¹⁹ Generally, consumer remedies for these violations include recovery for compensatory damages, recovery of punitive damages, recovery of attorney’s fees, and the option of filing a class action lawsuit. Prior to this, consumers were forced to sue merchants for torts or misrepresentations which were often hard to prove because consumers needed to prove affirmative misrepresentation of fact or intent to deceive.¹²⁰ However, there is substantial variation in mini-UDAP laws. For instance, each state’s UDAP statute varies in its coverage of deceptive or unfair acts (or both); exclusion of certain industries and transactions; and substantive rulemaking authority.¹²¹

Under state mini-UDAP laws, regulatory enforcement by private consumers can be difficult. To illustrate, although all states (except Iowa) allow consumers to enforce UDAP, Arizona, Delaware,¹²² Mississippi, Iowa,¹²³ South Dakota, and Wyoming impose a financial cost by denying consumers recovery of attorneys fees.¹²⁴ Michigan¹²⁵ and Rhode Island¹²⁶ exempt “consumer lending” from UDAP violations. These states do not enforce UDAP provisions on entities, which are already regulated by another body of law, in effect, gutting the statutory protections for consumer lending.

¹¹⁷ See Late fees, La. Rev. Stat. Ann. § 9:3527(1); Additional Charges, La. Rev. Stat. Ann. § 9:3529.

¹¹⁸ See Dee Pridgen, *The Dynamic Duo of Consumer Protection: State and Private Enforcement of Unfair and Deceptive Trade Practices Laws*, 81 Antitrust L.J. 911 (2017).

¹¹⁹ *Id.* at 917.

¹²⁰ *Id.*

¹²¹ *How well do states protect consumers*, NCLC (Mar. 2018), <https://www.nclc.org/images/pdf/udap/udap-report.pdf>.

¹²² The court in exceptional cases may award reasonable attorney’s fees to the prevailing party. Attorney’s fees may be assessed against the defendant only if the court finds that defendant has willfully engaged in a deceptive trade practice. 6 Del. C. § 2533.

¹²³ If the consumer is awarded actual damages because the person is determined to be in violation of this chapter, the court may award the consumer’s attorney reasonable fees. Iowa 714 H.5.

¹²⁴ *Consumer Protection in the States: A 50-State Evaluation of Unfair and Deceptive Practices Laws*, NCLC (2018).

¹²⁵ UDAP exempts transactions or conduct specifically authorized under laws administered by a regulatory body. See Mich. Comp. Laws Ann. § 445.904(1)(a). This exemption has been interpreted by a number of Michigan courts to exempt lending. See, e.g., *Molosky v. Washington Mut., Inc.*, 664 F.3d 109, 117-118 (6th Cir. 2011).

¹²⁶ The Rhode Island UDAP statute does not apply to “actions or transactions permitted under laws administered by” a state or federal regulatory body. See R.I. Gen. Laws § 6-13.1-4. In *Chavers v. Fleet Bank*, the R.I. Supreme Court interpreted this language as a blanket exclusion of creditors. 844 A.2d 666 (R.I. 2004).

In light of Dodd Frank’s key role for state governance in consumer protection laws, a few states have started to actively expand their mini-UDAP laws to cover “abusive” acts and practices as well. In 2018, Maryland substantively amended the Maryland Consumer Protection Act (“MCPA”) to include the prohibition of “unfair, abusive, or deceptive trade practices.”¹²⁷ In 2020, the California Consumer Protection Law expanded the state regulators’ purview by including new industries such as debt-relief companies, consumer credit report agencies, and debt collectors to better protect consumers from unlawful, unfair, deceptive, and *abusive* practices.¹²⁸

II. THE IMPLICATIONS OF BNPL CONSUMER LENDING PRACTICES

Despite the clear demand for these services, if these installment loans are to be provided to the consumers, there must be appropriate consumer protections in place to ensure that the lenders provide proper disclosures and consumers do not accumulate debt.¹²⁹ As indicated by the explosion of BNPL-related consumer complaints filed with the CFPB in 2021, this Part discusses how current BNPL lending practices of deceptive disclosures of consumer credit impact and abusive hidden fees are in violation of UDAAP.¹³⁰ In response, the federal UDAAP provision enforced by the CFPB and the UDAP provisions enforced by the FTC are the most applicable existing laws.

A. Deceptive Disclosure of Credit Reporting

First, BNPL raises an issue with deceptive disclosures that is of heightened concern because BNPL loans are not regulated as tightly as traditional credit products.¹³¹ BNPL lenders structure their loans to evade TILA regulations.¹³² But, to a varying degree, certain states are still able to require disclosure of loan terms under their licensing laws. So, the real issue lies in the blatant misrepresentation of the credit product as safe and “risk-free.”¹³³

The federal UDAAP law addresses this issue. BNPL lending

¹²⁷ Md. Code Ann., Com. Law § 13-101(k) (2010).

¹²⁸ Cal. Fin. Code §90000(b) (2020).

¹²⁹ See *supra* note 124.

¹³⁰ As demonstrated by the CFPB’s data research, consumer complaints against Afterpay, Klarna and Affirm rose significantly this year as compared to last year. In particular, approximately half of Affirm’s total consumer complaints from the last three years were made in between January to November of 2021. Consumer Complaint Database, CFPB (last visited Nov. 22, 2021), https://www.consumerfinance.gov/data-research/consumer-complaints/search/?chartType=line&dateInterval=Month&dateRange=1y&date_received_max=2021-11-22&date_received_min=2020-11-22&expandedRows=Credit%20reporting%2C%20credit%20repair%20services%2C%20or%20other%20personal%20consumer%20reports&lens=Overview&searchField=all&searchText=affirm&tab=Trends.

¹³¹ See *supra* note 124.

¹³² See *supra* note 64.

¹³³ See *supra* note 25.

practices largely fall under “deceptive acts or practices.”¹³⁴ A deceptive act is when an act or practice misleads or is likely to mislead the consumer; the consumer’s interpretation is reasonable under the circumstances; and the misleading act or practice is material.¹³⁵

Misrepresentation of a product-offering runs the risk of consumers not understanding the terms of BNPL financing before they make purchases. BNPL lenders’ primary deceptive misrepresentation is their highly advertised practice of not reporting BNPL credit to credit agencies, despite lenders still reporting missed payments to credit agencies. When a “Help Center” reads:

[This product] does not affect your credit score or credit rating. Your credit score can be impacted when somebody does a credit check on you or if you are reported as paying debts late; [...] we never do credit checks or report late payments.¹³⁶

Any reasonable consumer may believe that using the product will not affect their credit scores. However, despite the overtly risk-free message, some BNPL lenders reserve the right to forward delinquent accounts to debt collectors.¹³⁷ According to Credit Karma, “a debt in collections is one of the most serious negative items that can appear on credit reports because it means the original creditor has written off the debt completely.”¹³⁸ Therefore, current BNPL practices are deceptive because lenders are disproportionately shifting emphasis on consumer-friendly facets of the products without disclosing the associated material risks.¹³⁹

First, to determine whether an act actually misled the consumer, the totality of the circumstance is considered such as the implied representation or the omission of certain statements.¹⁴⁰ In *SMART Payment Plan*, the CFPB found that the provider engaged in deceptive practices because the product was marketed as financially beneficial to consumers when the provider was aware that it had no such effect.¹⁴¹ Similarly, some BNPL lenders intentionally advertise no credit checks and no reporting of late payments as protective of consumers’ credit health.¹⁴² However, when retaining the right to transfer delinquent accounts, the lenders are aware

¹³⁴ See *supra* note 120.

¹³⁵ See *supra* note 120.

¹³⁶ *Is using Afterpay bad for my credit score?*, AFTERPAY HELP CENTRE (2021), <https://help.afterpay.com/hc/en-au/articles/900003970646-Is-using-Afterpay-bad-for-my-credit-score>.

¹³⁷ BNPL lenders, including Affirm, Afterpay, Klarna and Zip, reserve the right to forward accounts to the debt collector, which can lead to aggressive debt collection and negative credit impact to consumers. Tara Bernard, *Consumers and Companies are Buying in on Pay Later*, NY TIMES (Sept. 3, 2021), <https://www.nytimes.com/2021/09/03/your-money/buy-now-pay-later-afterpay-affirm-amazon-square.html>.

¹³⁸ Clint Proctor, *What Should I know if have Debts in Collections?*, CREDIT KARMA (Apr. 13, 2021), <https://www.creditkarma.com/advice/i/accounts-in-collections>.

¹³⁹ When the consumer debt is transferred from the original creditor to the debt collection agencies, the debt is considered a new trade line on the consumer credit report, which indicates that debt is now under the control of the collection agency. Ben Luthi, *What are Tradelines and How Do They Affect You?*, EXPERIAN (2019), <https://www.experian.com/blogs/ask-experian/what-are-tradelines/>.

¹⁴⁰ See *supra* note 114.

¹⁴¹ Consent Order, In the Matter of: SMART Payment Plan, LLC, No. 2020-CFPB-0020 (Nov. 2, 2020) [hereinafter SMART Payment Plan Consent Order].

¹⁴² Nina Hendy, “Buy Now, Pay Later with No Credit Check Explained”, FORBES ADVISOR (Nov. 22, 2022), <https://www.forbes.com/advisor/au/buy-now-pay-later/no-credit-check-explained/>.

that consumer credit can be impacted to the detriment of the borrower.¹⁴³ Thus, the BNPL lenders deceptively market their products as “risk-free” to consumers while being fully aware that missed payments and subsequent delinquent accounts are not at all “risk-free.”

Next, to determine if the consumer’s interpretation was reasonable under the circumstance, the CFPB judges whether the misrepresentation was reasonable to the specific audience.¹⁴⁴ As articulated in *Newday Financial, LLC*, an identified member is a person toward whom the provider is soliciting or marketing to.¹⁴⁵ As noted earlier, BNPL is heavily marketed toward Millennials and Gen Z through celebrity features and TikTok partnerships.¹⁴⁶ Given this cohort of consumers and their demonstration of low financial literacy,¹⁴⁷ there is a strong argument that young consumers are unfamiliar with BNPL lenders’ rights to send over delinquent accounts to debt collectors.¹⁴⁸ The consumer’s reasonable misinterpretation of a “risk-free” credit product exposes the young borrower to lower credit scores because delinquent accounts transferred to debt collectors drive down credit scores.¹⁴⁹

Lastly, the deceptive act is material if the information is likely to affect a consumer’s choice or if the information is likely important to the consumer.¹⁵⁰ There is no doubt that if consumers knew that missed payments or delinquent accounts may affect their credit scores, then they would be more diligent about making timely payments.¹⁵¹ A Consumer Report showed that 43% of BNPL installment payments were late and incurred late fees.¹⁵² Of those, two-thirds of missed payments were because they lost track of the payment schedule, not because consumers did not have the financial means.¹⁵³ Had these delinquent consumers known that late payments jeopardize their credit worthiness, they might have rejected BNPL financing or made a greater effort to make timely payments.¹⁵⁴ Therefore, these supposedly “credit-safe” products are entirely deceptive.¹⁵⁵

¹⁴³ *Id.*

¹⁴⁴ *See id.*

¹⁴⁵ Consent Order, In the Matter of: Newday Financial, LLC, No. 2015-CFPB-0004 (Feb. 10, 2015) [hereinafter *Newday Financial Consent Order*].

¹⁴⁶ Joshua Bote, ‘Buy now, pay later’ is sending the Tiktok generation spiraling into debt, popularized by San Francisco tech firms,’ SFGATE, <https://www.sfgate.com/news/article/influencers-lead-Gen-Z-into-debt-17142294.php> (May 4, 2022).

¹⁴⁷ A TIAA study has shown that although financial literacy is low amongst all five generation, Gen Z and Millennials score the lowest. Paul Yakoboski, Annamaria Lusardi and Andrea Hasler, *2020 TIAA Institute-GFLEC Personal Finance Index (P-Fin Index)*, TIAA INSTITUTE (2020).

¹⁴⁸ *See supra* note 128.

¹⁴⁹ *See supra* note 129.

¹⁵⁰ *See supra* note 114.

¹⁵¹ *Id.*

¹⁵² Penelope Wang, *The Hidden Risks of Buy-Now, Pay-Later Plans*, CONSUMER REPORTS (Feb. 14, 2021).

¹⁵³ *Id.*

¹⁵⁴ *See supra* note 136.

¹⁵⁵ The FTC’s traditional 4P’s test is not entirely applicable because the BNPL lenders are not hiding the disclosure in fine print or engaging in similar deceptive behaviors; rather they are implying an idea to the consumers by heavily advertising a half-truth. Lesley Fair, *Full Disclosure*, FTC, (2014), <https://www.ftc.gov/news-events/blogs/business-blog/2014/09/full-disclosure>.

B. Unfair and Abusive Practice Concerning Fees

Second, BNPL lenders are engaging in an abusive and unfair practice by failing to properly disclose hidden fees related to product use. Currently, BNPL lenders heavily advertise their credit products as “4 interest-free payments” or “never pay interest.” In effect, the lenders offer to provide immediate and convenient access to credit at virtually no expense. However, lenders can impose surprise expenses through potential late fees. In addition, although not perpetrated by the lenders, consumers can be hit with hefty, hidden costs by their banks in the form of nonsufficient fund (NSF) and overdraft fees when BNPL lenders make automated withdrawals of consumers’ payments without prior payment authorization.

These practices create potential liability under the federal UDAAP provisions and state anti-deceptive laws.

Unfair

First, the lack of transparent disclosure about NSF and overdraft fees is unfair. When analyzing whether a practice is “unfair,” the Bureau balances the following factors: whether the act (1) caused or was likely to cause substantial injury to consumers; (2) which is not reasonably avoidable by consumers; and (3) that such injury was not outweighed by countervailing benefits to consumers or competition.¹⁵⁶

These fee practices are unfair because they cause substantial injury to the consumers. As the CFPB determined in its final rule in 2017 on payday loans, when a bank debit fails, the cost to consumers may be correspondingly high because the consumer will incur a NSF.¹⁵⁷ And, even if the payment is consummated, the bank may still charge an overdraft fee.¹⁵⁸ The same findings apply to BNPL loans by analogy.

Further, this harm is compounded in the BNPL context because some BNPL lenders engage in multiple withdrawal attempts. One BNPL lender’s collection policy states that when an automatic payment for an order fails, it will attempt to collect the payment from the other cards on the account.¹⁵⁹ Klarna, another BNPL lender, faces a Connecticut class action lawsuit in which the lead plaintiff claims that the lender failed to notify the consumer of the first withdrawal attempt (incurring a \$35 overdraft fee on a \$15.83 purchase payment) and a second withdrawal attempt on a different purchase (incurring another \$35 overdraft fee on a \$9.31 purchase payment).¹⁶⁰ In effect, the consumer paid a \$70 penalty for two purchases totaling \$26.14, which is substantial financial harm because the sum penalty was far greater than the actual purchase price.

¹⁵⁶ 12 U.S.C. § 5531(c)(1).

¹⁵⁷ Payday, Vehicle Title, and Certain High-cost Installment Loans, 82 Fed. Reg. 54,472 (Nov. 17, 2017).

¹⁵⁸ *Id.* at 54,582.

¹⁵⁹ *Does Afterpay have an automatic payment system?*, AFTERPAY HELP CENTER (2021),

<https://help.afterpay.com/hc/en-us/articles/217426326-Does-Afterpay-have-an-automatic-payment-system->

¹⁶⁰ The causes of action are common fraud and the violation of the Connecticut Unfair Trade Practices Act (CUPTA) which prohibits unfair competition and unfair and deceptive acts. *Najah Edmundson v. Klarna, Inc.*, No. 3:21-cv-00758, (D. Conn. June 2, 2021).

However, even a first withdrawal attempt without proper notice may cause substantial injury. In California, Afterpay faces another class action lawsuit for failing to notify consumers of the large overdraft and NSF fees associated with the use of the service.¹⁶¹ In *Miller v. Afterpay*, the lead plaintiff claims that the automatic payment that Afterpay deducted from her account, amounting to just over \$15, resulted in a \$35 overdraft bank fee.¹⁶² Therefore, the determination of unfair practices should be extended to instances when consumers incur NSF fees at the first withdrawal attempt without proper warning.

Second, consumers are unable to avoid the harm because they are largely unaware that an unsuccessful payment can lead to financial penalties from an outside institution.¹⁶³ Due to the nature of automated payments, consumers have limited control over authorizing stop-payments¹⁶⁴ and revoking a payment is generally costly and difficult; accordingly the harm is not reasonably avoidable by the consumer. Lastly, although automated withdrawal may be beneficial to both consumers and lenders by providing a speedy, predictable, and low-cost means of repayment, the injuries from a failed withdrawal in the form of NSF and overdraft fees outweigh the convenience.

Therefore, consistent with the CFPB's application of the "unfair" test as applied to payday lenders, current BNPL lenders' practices are unfair. Even in a situation where there is only one withdrawal attempt, the BNPL practice is unfair as defined by the Bureau because the consumer still (a) incurs a substantial financial harm that (b) is unavoidable because there were no prior warnings or disclosure and (c) the convenience of automated payments does not outweigh the consumer's financial distress.¹⁶⁵

1. Abusive Practices Regarding NSF and Overdraft Fees

BNPL lenders' hidden fee practices are abusive. Although "abusive" claims are rare,¹⁶⁶ injured BNPL consumers have a good argument that undisclosed NSF and overdraft fees are abusive under the UDAAP. The Bureau considers these factors to determine whether a practice is abusive: whether the act takes unreasonable advantage of the lack of understanding on the part of the consumer with regards to the material risks and costs, or

¹⁶¹ The cause of action is the violation of California's Unfair Competition Law (UCL) which prohibits Acts of unfair competition, including misrepresentations and omissions about the true nature of using "BNPL" services. See *Miller v. Afterpay US*, No. 3:21-cv-04032 (N.D. Cal. May 27, 2021).

¹⁶² See *id.*

¹⁶³ *Id.* at 11; *Klarna, Inc.*, No. 3:21-cv-00758.

¹⁶⁴ A consumer does have the right to a stop payment but she will have to notify her financial institution about stopping the preauthorized electronic fund transfer at least three business days before the scheduled date of the transfer. 12 C.F.R. § 1005.10(c).

¹⁶⁵ See *supra* note 140.

¹⁶⁶ Patricia A. McCoy, *The Question of A General Rulemaking To Define The "Abusive" Standard*, CFPB Symposium (June 19, 2019), https://files.consumerfinance.gov/f/documents/cfpb_mccoy-written-statement_symposium-abusive.pdf.

whether the act takes unreasonable advantage of the inability of the consumer to protect their interest in selecting or using a consumer financial product.¹⁶⁷ The current BNPL lenders’ practice, of encouraging automated withdrawals¹⁶⁸ without proper disclosure of financial penalties, takes unreasonable advantage of consumers ability to understand the material risk associated with the use of the product. This effectively deprives the consumer of her ability to protect her interests.

The lack of fee disclosures satisfies both the “unreasonable advantage” tests. Depending on the facts and circumstances, an issuer may take unreasonable advantage of consumers by failing to inform them of the product conditions and exploit their lack of understanding.¹⁶⁹ In 2014, the CFPB stated that credit card issuers might engage in abusive conduct if [they failed] to adequately alert consumers to the financial consequences of missing payments.¹⁷⁰ BNPL lenders engage in such abusive conduct by failing to properly disclose hidden and late fees associated with the failure of payment; this conduct often provides consumers with incomplete marketing materials that over-emphasize “cost-free” and “risk-free” loans.

In *Re Fort Knox Nat’l Co.*, the Bureau further concluded that the lack of disclosure took unreasonable advantage of consumers’ ability to protect their interests because the consumers were unable to take steps to avoid the charges.¹⁷¹ While some BNPL lenders send SMS text messages before an automated withdrawal, this practice acts more as a notification of withdrawal rather than seeking consent for withdrawal.¹⁷² Additionally, consumers cannot easily revoke their payments, which leaves consumers with little to no recourse to protect their interest.¹⁷³ Therefore, the current BNPL practice of payment withdrawal without disclosures of the potential consequences of a failed payment is abusive because it unreasonably takes advantage of borrowers.

2. Abusive Practices Regarding Late Fees

Lastly, BNPL lenders’ practice of collecting excessive late fees is an abusive practice. When determining if a practice is abusive, the Bureau examines whether the lender takes unreasonable advantage of the lack of the consumer’s ability to understand the terms and conditions of the product.¹⁷⁴ Currently, Afterpay has a late fee policy stating that the lender only charges “one late fee per installment.”¹⁷⁵ However, the same lender allows the consumer to open multiple installment purchases on one

¹⁶⁷ Dodd-Frank Act, § 1036(a)(1)(B), 12 U.S.C. § 5531(d)(1).

¹⁶⁸ Currently, a lender advertises their automatic payment system as the “most convenient” way to pay because “we [the lender] do the rest.” *How do payments work?*, AFTERPAY (Jan. 19, 2022), <https://help.afterpay.com/hc/en-us/articles/360016052892-How-do-payments-work->.

¹⁶⁹ CFPB, Marketing of Credit Card Promotional APR Offers, CFPB Bull. 2014-02 (Sept. 3, 2014).

¹⁷⁰ 12 C.F.R. § 1006.14.

¹⁷¹ Consent Order, In *Re Fort Knox Nat’l Co.*, No. 2015-CFPB-008 (Apr. 20, 2015) [hereinafter *Fort Knox Consent Order*].

¹⁷² *Id.*

¹⁷³ On the Better Business Bureau, a consumer stated that despite her efforts to stop payment, she had to go so far as to lock her form of payment to make sure that the lender did not continue to make automated withdrawal. Customer Review, AFTERPAY, INC. (Dec. 8, 2021), <https://www.bbb.org/us/ca/san-francisco/profile/payment-processing-services/afterpay-inc-1116-897251/customer-reviews>.

¹⁷⁴ See *supra* note 50.

¹⁷⁵ *How do Payments Work*, AFTERPAY HELP CENTER (last updated Jan. 22, 2022), <https://help.afterpay.com/hc/en-us/articles/360016052892-How-do-payments-work->.

account, as demonstrated by *Miller v. Afterpay*.¹⁷⁶ In turn, when the consumer misses one due date on an account applicable to different installment purchases, the lender may penalize the consumer with multiple late fee charges.

In *Fort Knox*, the Bureau concluded that when a service provider does not adequately disclose the existence of specific fees and does not notify consumers when they incur said fees, the provider took unreasonable advantage of this lack of knowledge by charging millions of dollars to consumers.¹⁷⁷ Here, BNPL lenders do not properly disclose the financial ramifications of one missed payment because the disclaimer, “one late fee per installment,” is not stated on either the consumer’s payment schedule or the terms and agreements of the loan.¹⁷⁸ Instead, this information is only available through manual research on the lender’s website.¹⁷⁹ As such, a reasonable consumer may assume that one missed payment will only incur a one-time \$7 late fee to her account instead of a \$7 late fee charge per installment purchase. Therefore, by taking unreasonable advantage of consumers’ lack of ability to understand, BNPL lenders are profiting from compounded late fees.

With the increasing scrutiny around BNPL practices, a BNPL lender, Afterpay, points to its steady decrease of late fees attributable to its total income as indicative of its “inbuilt customer protections and budget-focused, differentiated, business model.”¹⁸⁰ However, this is a faulty analysis of the quantitative data because Afterpay is not properly accounting for its significant growth in total income, which is likely attributable to a 108% increase in merchant fees collected.¹⁸¹ When solely examining the numerical values of revenue generated from late fees, Afterpay’s financial statement shows the opposite – an increase of late fees collected. In 2020, Afterpay generated \$69 million from late fees.¹⁸² In 2021, Afterpay generated \$87 million from late fees which marks a nearly 28% increase of late fee collection.¹⁸³

As BNPL competition rises, there are some signs that the marketplace is curing itself of predatory practices because some lenders have altogether dropped late fees.¹⁸⁴ However, there is still room for regulatory supervision because compounded late fee charges are abusive.

¹⁷⁶ See *supra* note 145.

¹⁷⁷ Fort Knox Consent Order, *supra* note 151, at 8.

¹⁷⁸ Afterpay, *What do I do if the automatic payment fails?*, AFTERPAY HELP CENTRE (2022), <https://help.afterpay.com/hc/en-us/articles/218320643-What-do-I-do-if-the-automatic-payment-fails->.

¹⁷⁹ *Id.*

¹⁸⁰ See *supra* note 25.

¹⁸¹ See *id.*

¹⁸² See *id.*

¹⁸³ See *id.*

¹⁸⁴ PayPal announced that it will no longer charge customers late fees when they miss payments on BNPL purchases, globally. This change was a bid to ensure that consumers are not taking on more debt than they may handle. Anna Irrera, *PayPal scraps late fees for buy now, pay later purchases*, Reuters (Aug. 18, 2021), <https://www.reuters.com/technology/paypal-scraps-late-fees-buy-now-pay-later-purchases-2021-08-18/>.

III. PROPOSED REFORMS

Current state law fails to sufficiently prevent and remedy consumer harm from BNPL loans because the law fails to provide uniformed protections against deceptive disclosures and hidden fees. However, the CFPB has federal enforcement and regulatory authority over BNPL lenders under the Federal UDAAP provisions.

With regards to deceptive credit reporting disclosures, the CFPB should write comprehensive consumer education materials to increase consumers’ financial literacy about BNPL loans.¹⁸⁵ On December 2, 2021, in line with this recommendation, the Bureau posted a frequently asked question discussion on the topic of BNPL lenders’ rights to transfer delinquent accounts to collection agencies. In the FAQ it explained to consumers the detrimental effects of missing a payment.¹⁸⁶ Furthermore, although the implications of Equifax’s decision to include BNPL data on consumer credit reports are yet to be determined, the CFPB should publish additional material so that consumers understand that “no credit check” does not necessarily mean “no credit impact.”¹⁸⁷ Along with the informative material, the CFPB should release guidance as to how lenders may revise their marketing materials to not misrepresent the negative credit impact associated with product use.

The issue of hidden fees requires higher enforcement pressure because of the financial toll overdraft and NSF fees exact on unsuspecting consumers. Consumers are blind-sided by these financial penalties. To remedy the issue of surprise NSF and overcharge fees, the CFPB should mandate a payment authorization rule and a withdrawal attempt limitation.¹⁸⁸ This new rule would prohibit BNPL lenders from making automated withdrawals without prior SMS authorization and prohibit lenders from making more than one attempt at withdrawal.

Unfortunately, rulemaking can be a timely and burdensome process during which consumers continue to be harmed.¹⁸⁹ Therefore, pending the Bureau’s findings from the ongoing investigation against five prominent BNPL lenders, the CFPB should create consent orders. In the consent orders, the CFPB should restrain and enjoin lenders under the UDAAP from further misrepresentation of the BNPL product and ensure that all marketing material clearly, prominently, and accurately describe the material costs, conditions, and limitations associated with the

¹⁸⁵ This article finds that with higher financial literacy, consumers are more likely to reduce the perceived benefits of BNPL whereas with lower financial literacy, consumers are more likely to increase the benefits and decrease the risks. Paul Gerrans, Dirk Baur, and Shane Slater, *Fintechs and Responsibility: Buy-now-pay-later-arrangements*, THE UNIVERSITY OF WESTERN AUSTRALIA, (2021).

¹⁸⁶ *Will a Buy Now, Pay Later (BNPL) loan impact my credit scores?*, CFPB (Dec. 2, 2021), <https://www.consumerfinance.gov/ask-cfpb/will-a-buy-now-pay-later-bnpl-loan-impact-my-credit-scores-en-21117/>.

¹⁸⁷ Jennifer Surane, *Equifax to Include Buy-Now, Pay-Later Purchases on Credit Reports*, BLOOMBERG (Dec. 20, 2021), <https://www.bloomberg.com/news/articles/2021-12-20/equifax-to-include-buy-now-pay-later-purchases-on-credit-report>.

¹⁸⁸ This action would be modeled after the Bureau’s rulemaking for payday lenders. See *Payday, Vehicle Title, and Certain High-cost Installment Loans*, 82 Fed. Reg. 54,472 (Nov. 17, 2017).

¹⁸⁹ At the beginning of a rulemaking, the Bureau will receive suggestions from a variety of sources to inform the drafting of the proposed rule. Then, the proposed rule is published in the Federal Register or on the CFPB’s website. Following this, the CFPB publishes an interim final rule and subsequently opens the public comment period in which written comments are posted on the public rulemaking docket. Leonard Kennedy, *Promoting Openness in CFPB rulemaking*, CFPB Blog, (Aug. 19, 2011).

product.¹⁹⁰

Given the market interest in these fast and flexible loans, it may be oppressive to overburden lenders with costly regulatory provisions. In order to better protect consumers while better regulating lenders, the Bureau should set industry standards. These standards should include pursuing investigations, sending warning letters, and issuing consent letters to signal to the broader BNPL marketplace that lenders should comply with the UDAAP provisions. Presently, the Bureau has only ordered an investigation of BNPL lenders and opened public comments.

On December 16, 2021, the CFPB issued a series of orders to five BNPL companies citing concerns of accumulating debt, regulatory arbitrage, and consumer disclosure.¹⁹¹ The Bureau ordered the lenders to “submit information so that [the Bureau] can report to the public about industry practices and risks.”¹⁹² On December 20, 2021, as a response to the CFPB investigation, Equifax announced that payments on BNPL will be added to consumer credit reports in 2022.¹⁹³ On January 12, 2022, the CFPB opened public comments to learn more about the buyers’ experience, the merchants’ experience and ways in which the BNPL market can be improved.¹⁹⁴ On September 15, 2022, the CFPB announced the results of its investigation and stated that the rise of the BNPL market calls for further protections and protocol in order to ensure a baseline of consumer protection.¹⁹⁵ The four areas of focus are: (1) ensuring the proper and accurate credit reporting from BNPL lenders, (2) designing appropriate supervisory examinations of BNPL lenders, (3) identifying the extent of data surveillance of BNPL consumers, and (4) including BNPL loans when calculating the average household debt burden.¹⁹⁶

IV. CONCLUSIONS

CFPB’s September BNPL report and Director Chopra’s call for stronger regulatory provisions show rapid development in the BNPL landscape. In the upcoming year, consumers can expect to see increased disclosures regarding deceptive credit reporting and surprise hidden costs associated with the use of BNPL products. In addition, there is great anticipation for innovative regulatory provisions and guidance under the new Director of the CFPB.

During his term as the former Commissioner of the FTC, CFPB

¹⁹⁰ See *supra* note 157.

¹⁹¹ *Id.*

¹⁹² *Id.*

¹⁹³ *Equifax First to Formalize Inclusion of “Buy Now, Pay Later” payment information in Consumer Credit Reports*, Equifax Press Release (Dec. 20, 2021), <https://investor.equifax.com/news-events/press-releases/detail/1204/equifax-first-to-formalize-inclusion-of-buy-now-pay>.

¹⁹⁴ Ashwin Vasan, *Our Public Inquiry on Buy Now, Pay Later*, CFPB BLOG (Jan. 12, 2022), <https://www.consumerfinance.gov/about-us/blog/our-public-inquiry-buy-now-pay-later/>.

¹⁹⁵ CFPB, *Director Chopra’s Prepared Remarks on the Release of the CFPB’s Buy Now, Pay Later Report*, CFPB NEWSROOM (Sept. 15, 2022), <https://www.consumerfinance.gov/about-us/newsroom/director-chopras-prepared-remarks-on-the-release-of-the-cfpbs-buy-now-pay-later-report/>.

¹⁹⁶ *Id.*

Director Chopra created FTC’s Technology Enforcement Division. The goal of the division is to monitor competition and investigate potential anticompetitive conduct in markets in which digital technology is an important facet of the competition.¹⁹⁷ As BNPL business models are the “new version[s] of the old layaway plan[s],” Director Chopra is particularly well-positioned to wield the agency’s rulemaking, supervisory, and enforcement authority against BNPL lenders who continue to operate within regulatory loopholes.¹⁹⁸

¹⁹⁷ *Technology Enforcement Division*, FTC (2019), <https://www.ftc.gov/about-ftc/bureaus-offices/bureau-competition/inside-bureau-competition/technology-enforcement-division>.

¹⁹⁸ *Consumer Financial Protection Bureau Opens Inquiry into “Buy Now, Pay Later” Credit*, CFPB NEWSROOM (Dec. 16, 2021), <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-opens-inquiry-into-buy-now-pay-later-credit/>.