

Article Information

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The DL on BNPL: ASIC's update on the Buy-Now-Pay-Later industry

ASIC's new Report 672 identifies the growth and evolution of the buy now pay later industry, the impact of buy now pay later arrangements on consumers and recent regulatory developments.

On 16 November 2020, ASIC released their much-anticipated updated report on the booming buy-now-pay-later industry through Report 672 'Buy-Now-Pay-Later An Industry Update' (**REP 672**). The buy-now-pay-later (**BNPL**) industry has been growing exponentially over the past few years with more and more consumers turning to this method of payment as an alternative to traditional forms of credit, such as credit cards.

There has been much controversy concerning BNPL, with many questioning whether it falls within the definition of 'credit' or whether it can be merely considered as 'electronic layby' for the modern world. While on one hand the views of Senator Andrew Bragg and the findings from the Interim Report evidence a support for a self-regulatory framework, others such as Matt Comyn, CEO of Commonwealth Bank Australia was quoted as saying "when you open a buy now, pay later account and it said you are approved for \$1000 that sounds like credit to me...We believe that regulation is inevitable but not imminent".^[1] This echoes the wide-held sentiment that BNPL should be treated as credit and accordingly, comply by the prescriptive credit laws.

Growth and evolution of BNPL

BNPL accounts

ASIC found that the number of active BNPL accounts held by BNPL providers increased steadily each financial year from the 2015/2016 financial year (around 487,000 active accounts) to the 2018/2019 financial year (around 3.7 million active accounts). As at June 2019, the 6 BNPL providers who participated in the review had collectively approved 6.1 million accounts. An 'active account' is a BNPL account where at least 1 transaction has occurred during the financial year, so it is a good indication of how many people have entered into a BNPL arrangement during a financial year.

BNPL transactions

Similarly, there has been an increase in the **number** of BNPL transactions. There has been a 75% increase in BNPL transactions from the 2017/2018 financial year to the 2018/2019 financial year. This is an increase from 1.9 million as at June 2018 to 3.4 million in June 2019. This 1.5 million increase in the course of 1 year indicates the rising popularity of BNPL. Not surprisingly, the number of BNPL transactions seem to reflect seasonal trends. ASIC has noted that there seems to be an increase in BNPL transactions in the lead up to Christmas in December each year.

Matching the increase in the number of BNPL transactions, the **value** of these transactions have also continued to increase. ASIC found that there was a 79% increase in the actual value of the BNPL transactions. From the 2017/2018 financial year to the 2018/2019 financial year there was an increase from \$3.1 billion to \$5.6 billion. ASIC found that Afterpay dominated the market with 73% of the value of BNPL transactions in the 2018/2019 financial year.

Outstanding balance

REP 627 also shed some light concerning the outstanding balance or rather, the total balance of outstanding debt from BNPL arrangements. Along with the increased number and value of BNPL transactions, the total outstanding balance of

BNPL accounts has also increased. However, this was at a more modest rate of 53% - from \$907 million in June 2018 to \$1.4 billion as at June 2019.

Revenue

The total revenue of the 6 BNPL providers increased by 50% from \$266 million in the 2017/2018 financial year to \$398 million in the 2018/2019 financial year. Interest is not charged in standard BNPL arrangements. Instead revenue is generated through merchant fees, missed payment fees, establishment fees and account-keeping fees. However, the revenue sources differ between the 6 BNPL providers, as these depend on the business models of each provider.

Diverse business models

All 6 BNPL providers were identified as having differences between the maximum loan amount and the loan terms. There was also a difference in the average transaction value for each BNPL provider. The providers with the lower average transactional value (such as Afterpay, with the lowest average transaction value of \$147) was used for lower value items (such as clothing). Whereas BrightePay (with the highest average transaction value of \$8,222) was used for big ticket items, such as home improvement products.

Future of credit?

ASIC's report found that over the same period as the BNPL industry continued to grow, the total value of personal credit card transactions plateaued, seeing a shift away from 'traditional' credit offerings. There is a converse trend between the growth in the value of BNPL arrangements versus the growth in the value of personal credit cards. The BNPL market's strong growth could suggest a shift towards consumers using BNPL arrangements instead of more traditional forms of credit, such as credit cards.

Growth in 2020

Despite the disruptions caused to everyday life and the economy by COVID-19, the data collected by ASIC from the BNPL providers show that the BNPL industry continued to grow in 2020. The number of transactions made, number of transacting users and the total value of transactions have each grown by more than 20% in the 12 months from June 2019 to June 2020.

Impact of BNPL arrangements on consumers

ASIC found that most BNPL providers charged consumers 'missed payments fees' whenever they missed a payment. REP 627 noted that roughly 21% of BNPL consumers surveyed had missed a payment in the past 12 months. Of those consumers who admitted to missing a payment, some interesting points ASIC discovered were:

1. 47% were aged between 18-29;
2. 39% also held a small amount credit contracts and/or medium amount credit contracts;
3. 34% made at least 6 BNPL purchases in the previous 6 months; and
4. 55% had used at least 2 different BNPL arrangements in the previous 6 months.

In that same financial year, most BNPL transactions were completed by consumers aged under 35. Of those transactions, 67% that incurred 'missed payment fees' were also by consumers aged under 35. Generally, ASIC found that the number of 'missed payment fees' incurred by consumers grew at a similar rate to the total number of BNPL transactions.

Not surprisingly, the growth in these fees meant that between June 2016 to June 2019, 'missed payment fees' made up:

1. about 15% of total revenue of the BNPL providers; and
2. about 44% of consumer revenue from all sources, including account-keeping fees.

Concerns for consumers

In a survey ASIC conducted, the regulatory body found:

1. 20% of consumers surveyed indicated that they had to cut back on or went without essentials (such as meals); and
2. 15% of consumers surveyed said they had to take out an additional loan.

Of these 2 groups of consumers surveyed, about 50% were in the 18-29 age group.

ASIC also took an alternate view when considering the impact of BNPL arrangements on consumers by looking at the credit card accounts of BNPL users from 4 major financial institutions. ASIC found that BNPL credit card users were more

likely to incur interest charges on their credit card and have higher credit limit use.

Surcharging

All BNPL providers who participated in ASIC's review charged varying fees to their partnered merchants. REP 627 found that BNPL providers generally contractually prohibit merchants from increasing the cost of goods and services to consumers who use BNPL arrangements.

It is unlikely that surcharging occurs across the whole BNPL industry, as surcharging is not possible where the pricing of goods and services are transparent and standardised.

To prevent surcharging, ASIC and ACCC have written to over 5,000 merchant partners of BNPL providers (in industries which ASIC believed were more likely to engage in surcharging) warning them that it is illegal to mislead or deceive consumers about the costs of goods and services.

As part of its periodic review of retail payments regulation commenced in November 2019, the Reserve Bank asked for stakeholder views on the 'no-surcharge' rules typically imposed by BNPL providers on merchants. However, as with many things this year, due to COVID-19, the RBA put the review temporarily on hold and it is now expected to be completed in 2021.

Regulatory developments

Design and distribution obligations (DDO)

From October 2021, design and distribution obligations will apply to most products regulated by ASIC, including BNPL arrangements. BNPL arrangements are currently regulated as credit under the ASIC Act and are subject to ASIC's new Product Intervention Order (**PIO**) power.

BNPL providers will be required to use resources such as industry knowledge, information about their users and other data to define the target market for their particular BNPL arrangement and also to set distribution conditions in the determination and in considering the reasonable steps that are likely to result in distribution of the arrangement being consistent with its target market.

BNPL providers must review and monitor the outcomes of their arrangement and consider whether changes are required to the arrangement itself, how it is sold and to whom it is being sold. ASIC's review highlighted that while BNPL arrangements have generally been embraced by consumers, there are always some consumers who may encounter financial difficulty, as with most credit products. If a BNPL provider offers arrangements which are designed and marketed as offering cost-free, or low-cost access to deferred payment, this should be a main consideration for the BNPL provider in terms of their DDO. For example, if a BNPL provider's data reveals that the fees it is charging is having a significant impact on consumers, they will need to consider why this is occurring and how this can be addressed.

Industry self-regulation

The Australian Finance Industry Association announced in December 2019 that it is developing an industry code of practice for BNPL providers (**BNPL Code**). This will respond to the finding of ASIC's 2018 report and the recommendations by the Senate Economics References Committee inquiry.

If effective, the BNPL Code can play an important part in delivering benefits to both consumers and subscribers to the code. This will improve consumer confidence in the BNPL industry.

Product intervention power

ASIC's REP 672 has provided informative insight into the rapidly developing BNPL industry. As it continues to grow in popularity surpassing traditional forms of credit, it is likely that concerns with how and if it should be regulated will continue to grow as well. It is hoped that the proposed BNPL Code will ease concerns noted in ASIC's report and strike a balance between allowing consumers to benefit from BNPL arrangements while providing a guideline as to how BNPL providers subscribed to the BNPL Code should operate in order to safeguard consumers' rights.

[1] James Frost, 'CBA CEO Comyn says property investors will return' *Australian Financial Review*, 18 November 2020.