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Which?, 2 Marylebone Road, London, NW1 4DF  
Date: 1<sup>st</sup> December 2020  
Response to: Call for Input: The Woolard Review

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## Consultation Response

### Which? response to FCA Call for Input: The Woolard Review

#### Summary

- Which? welcomes the opportunity to respond to the Woolard review. The review is particularly pertinent given the current context, with people financially impacted by coronavirus turning to credit to support them through this difficult time. As households become stretched during the pandemic, we are concerned about the risk of an increasing reliance on forms of unsecured credit when aspects of the market may not be working well for consumers.
- We are supportive of innovation in the unsecured credit market as a way of delivering benefits to consumers through useful new products and services. However, regulation of the unsecured credit market must balance innovation with consumer protection.
- Unregulated Buy Now, Pay Later services are becoming increasingly popular, with the market expected to grow over the next few years. Which? has concerns about certain structural features of this market including questions over transparency. The apparent lack of consumer protections compared to other regulated unsecured credit products needs to be addressed.
- We are therefore calling on the Woolard review to recommend to the FCA Board that Buy Now, Pay Later products are formally regulated.
- Which? has been supportive of the FCA's temporary guidance to support those experiencing financial difficulties during the coronavirus pandemic. The FCA should consider the broader applications of this guidance. In particular, it should consider how well credit referencing is working for consumers and reducing the time taken to process forbearance complaints.

#### Introduction

Which? welcomes the opportunity to respond to the Woolard review. Now more than ever is an important time to take stock of the unsecured credit market. The coronavirus pandemic has impacted the finances of millions of people, with Stepchange now estimating that 4.9 million people have borrowed to make ends meet since the beginning of the pandemic.<sup>1</sup> Qualitative insights from our research partners at Blue Marble suggest that consumers at the sharp end of the pandemic anticipate making greater use of credit, especially in the run-up to Christmas.

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<sup>1</sup> StepChange (2020) Tackling the coronavirus personal debt crisis. Available at: [https://www.stepchange.org/about-us/campaigning-for-you/tackling-covid-debt.aspx?dm\\_i=VD3,74G6K,U3SOG7,ST9PS,1](https://www.stepchange.org/about-us/campaigning-for-you/tackling-covid-debt.aspx?dm_i=VD3,74G6K,U3SOG7,ST9PS,1)

Even prior to the pandemic access to credit was important for a significant proportion of consumers. Our Everyday Finances report found that 42% of people would find it difficult to live without the ability to pay for things on credit.<sup>2</sup> Innovation in this space is undeniably beneficial to consumers, bringing about helpful features that can aid in accessing and managing credit. However, innovation must be balanced with consumer protections. It is important that consumers can access redress if things go wrong and that companies act in their best interests.

### **The coronavirus pandemic has impacted consumer's use of credit**

The coronavirus pandemic has undoubtedly harmed some consumers' financial wellbeing, with many consumers seeing their finances becoming stretched as a result of the crisis. As a result, we are expecting to see increasing numbers of consumers turning to credit over the coming months to help them cope with changes to their financial circumstances outside of their control.

Qualitative insights from our research partners at Blue Marble have shed light on the different impact that coronavirus is having on credit use. Some consumers have seen their financial situation stay the same or even improve over the course of the pandemic, allowing them in some cases to pay off credit card debt. However, other consumers have found themselves in more precarious financial positions. For some, the pandemic has eroded savings buffers, prompting an increase in borrowing. We have seen some using credit cards and store cards increasingly for grocery shopping, further indicating that some are struggling with their finances.

A minority of the households in our sample are in a very precarious financial position, with those who have lost their jobs being particularly worried about keeping up with bills. For those who are in this situation, many are finding it stressful or emotionally disruptive, prompting questions about their self-worth. In response to this precarity, less financially secure consumers described planning to use credit more or for the first time. For some this was to cover their day-to-day expenses. For instance, a participant describes using credit to pay for their car insurance. Others were focused on the holiday season and planned to use credit as a way of providing a 'normal' Christmas for their families.

These insights echo findings by Stepchange, who have seen an increase in the number of consumers seeking credit. Since the beginning of the outbreak, 33% (4.9 million) of those negatively affected by coronavirus have borrowed, compared to 26% in May.<sup>3</sup> The pandemic has impacted some groups more than others, with BAME and young people particularly likely to have borrowed.

Some consumers may already be struggling to make repayments: Which? research found that increasing numbers of people reported having defaulted on a payment (from 3.8% in September to 5.7% in October).<sup>4</sup> We also expect many consumers to struggle in the longer term, with Stepchange estimating that there are 2.87 million people affected by coronavirus who are now at high risk of long-term debt problems.<sup>5</sup>

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<sup>2</sup> Which? (2019). Everyday Finances Report. Available at: <https://www.which.co.uk/policy/money/4348/everydayfinances>

<sup>3</sup> Stepchange (2020) Tackling the Coronavirus Personal Debt Crisis. Available at:

<https://www.stepchange.org/Portals/0/assets/pdf/tackling-the-coronavirus-personal-debt-crisis.pdf>

<sup>4</sup> *ibid.*

<sup>5</sup> *ibid.*

## The emergence of Buy Now, Pay Later

Buy Now, Pay Later (BNPL) has emerged as an increasingly popular product over the last few years, with several new entrants to the market such as Klarna, Laybuy and Clearpay. According to a Compare the Market survey, one in five shoppers have used a BNPL service over the past year.<sup>6</sup> There is also some evidence that some consumers have been using these products as a result of the pandemic: a recent Which? survey found that 16% of people have used BNPL because of the impact the pandemic has had on their finances.<sup>7</sup> These companies offer people the ability to spread out the costs of goods and services interest-free, usually giving the option to pay after 30 days or in instalments. Unlike other products which typically charge interest, the new BNPL firms tend to make money by charging the retailer commission for every purchase made using their service. As well as the more well-known players in this market, there are other innovations in the space such as Flava, a BNPL Supermarket.<sup>8</sup>

Which? has been monitoring this market for some time and is currently undertaking some consumer research. We will provide this research to the FCA as soon as it is available.

Which? has concerns about some of the features of this market. We see four areas of potential harm:

- **Overspending:** There are early signs that BNPL products encourage overspending. BNPL firms themselves market their products to retailers based on their ability to increase spending. We are concerned that the design of these products could cause harm as a result, with vulnerable consumers particularly at risk.
- **A lack of transparency:** There are reports of considerable inconsistencies on the impact on credit ratings, the imposition of late fees and the use of debt collection agencies.
- **A lack of regulatory oversight:** Consumers can find it confusing to understand when products are regulated and when they are not. A recent Which? Survey found that 40% of consumers incorrectly thought that all BNPL are regulated<sup>9</sup>.
- **Consumer Protection:** There are key gaps in consumer protection for consumers using BNPL products, particularly when compared to similar regulated products. Which? has already heard reports of consumers struggling to obtain refunds from BNPL firms.

## The design of Buy Now, Pay Later products may lead to overspending

*'If things are easier to do, it can cause harm [...] Anyone that makes it easy to spend a lot of money needs to enable controls as well so that customers can protect themselves'* - Employee at a UK challenger bank<sup>10</sup>

A key feature of new Buy Now, Pay Later products is that they remove much of the friction from the process of taking out credit. This feature may be beneficial to some consumers, as it allows

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<sup>6</sup> Which? (2020) Can shopping with Klarna, Clearpay or Laybuy hurt your credit score? Available at: <https://www.which.co.uk/news/2020/01/can-shopping-with-klarna-clearpay-or-laybuy-hurt-your-credit-score/>

<sup>7</sup> Which? survey of 2001 UK adults, conducted between 13th-15th October 2020

<sup>8</sup> Which? (2020) Flava: new 'buy now, pay later' supermarket that lets you spread the cost of groceries. Available at: <https://www.which.co.uk/news/2020/10/flava-the-buy-now-pay-later-supermarket-that-lets-you-spread-the-cost-of-groceries-what-are-the-risks/>

<sup>9</sup> Which? survey of 2001 UK adults, conducted between 13th-15th October 2020

<sup>10</sup> Which? (2019). Everyday Finances Report. Available at: <https://www.which.co.uk/policy/money/4348/everydayfinances>

them to take out credit quickly and simply. However, the low-friction design of BNPL credit may cause harm to some consumers. Lower friction has been documented to cause issues for consumers, particularly if it leads to them taking on debt without fully considering whether they can pay it back.<sup>11</sup>

We are concerned that these products may make it more difficult for consumers to budget and could lead to poor financial decision making. BNPL companies themselves have published research suggesting that their products encourage consumers to spend more. For example, Clearpay claims that companies using its services increase sales by 22% and order value by 30% on average.<sup>12</sup> Klarna makes similar claims, stating that it can boost the average online store's sales by 30% and the average spend by 30%.<sup>13</sup> We have seen some reports of consumers getting into significant amounts of debt using these services. Our engagement with debt charities suggests that the number of people seeking debt advice with BNPL debt has increased over the last two years.

Vulnerable consumers may be particularly susceptible to harms from overspending. Recent research by the Money and Mental Health Policy Institute found that BNPL products can be particularly detrimental to people with mental health problems. This is because common symptoms of mental health problems like increased impulsivity and poor memory can make it harder to keep track of spending and to resist making purchases online.<sup>14</sup>

The FCA should assess the design of these products to gauge whether they encourage consumers to spend more money than they can afford to pay back.

### **There is a lack of transparency with BNPL products**

We are concerned with the lack of transparency for some of these products. Some previous research has flagged that BNPL firms do not always give clear information about their products.<sup>15</sup> For example, there is no information given about the consequences of non-payment at checkout,<sup>16</sup> except for the terms and conditions. However, terms and conditions can be difficult for consumers to understand<sup>17</sup> and many consumers do not read the terms and conditions.<sup>18</sup> Without greater transparency, some consumers may use BNPL products without fully understanding what the implications might be for their finances.

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<sup>11</sup> Money and Mental Health Policy Institute (2017) Fintech for Good. Available at: <http://www.moneyandmentalhealth.org/wp-content/uploads/2017/07/Fintech-for-good-report.pdf>

<sup>12</sup> Which? (2020). Shopping Temptation: The new buy now, pay later. Available at: [http://intranet.which.co.uk/magazines/which/2020/06\\_June/p34-37\\_Buy\\_now\\_pay\\_later\\_R3.pdf/](http://intranet.which.co.uk/magazines/which/2020/06_June/p34-37_Buy_now_pay_later_R3.pdf/)

<sup>13</sup> Money.co.uk (2020). Shop Now, Stress Later: Are millennials living through "generation debt trap"? Available at: <https://www.money.co.uk/guides/generation-debt-trap>

<sup>14</sup> Money and Mental Health Policy Institute (2020).

<sup>15</sup> HyperJar (2020) Research reveals attitudes to buy now, pay later deals and debt. Available at: <https://www.credit-connect.co.uk/consumer-news/research-reveals-attitudes-to-pay-now-buy-later-deals-and-debt/>

<sup>16</sup> Go Fund Yourself (2020) KlarNaa Campaign. Available at: <https://www.gofundyourself.co/bnpl>

<sup>17</sup> FCA (2014). Consumer Credit Research: Low Income Consumers. Available at: <https://www.fca.org.uk/publication/research/optimisa-research-low-income-report.pdf>

<sup>18</sup> Which? (2020). Member Insights Report: Buy Now, Pay Later Insights.

This issue is exacerbated by the fact that the design of these products can vary significantly by provider. For example, products often have different levels of late fees, different credit score searches and treat consumers differently if they fall into arrears.<sup>19</sup> (Please see attached annexes for further information). It can be confusing for consumers to understand and navigate the differences between these products, which risks leaving potentially vulnerable consumers in a detrimental situation.

Furthermore, many retailers only partner with one BNPL provider, meaning that consumers cannot shop around for the best BNPL deal. This means that consumers may not be able to pick the BNPL provider with the best terms and conditions for them, even if they do have a good understanding of the product.

### **BNPL products should be regulated by the FCA**

Many of these BNPL products are not regulated by the FCA.<sup>20</sup> As a result of the concerns we have highlighted above, there is the possibility of consumer harm and the FCA being unable to intervene appropriately.

Whilst BNPL and any other innovative payment methods that emerge may well increase competition in the market, it is clear that the regulation is needed to ensure that this does not come at the expense of adequate protection and redress for the consumers.

We are also concerned that the lack of regulation will cause confusion for consumers, who may assume that, like many other products, BNPL products are FCA regulated. A recent Which? survey found that 40% of consumers think that Buy Now, Pay Later products are regulated by the FCA.<sup>21</sup> This confusion may be particularly relevant where companies offer both regulated and unregulated products, as is the case with Klarna. The FCA should consider carefully the experiences of consumers and assess whether consumers' assumptions about whether a product is regulated is leading to harm.

Our view is that BNPL products should be regulated by the FCA. Giving the FCA the powers to regulate the BNPL market would allow it to more effectively monitor the treatment of consumers by BNPL firms. It would also allow the FCA to intervene where harms do emerge in the market. Even if harms in this market are relatively small at present, regulatory oversight is needed to ensure that harms can be addressed in the market as they emerge. This is especially important as the use of BNPL products is projected to increase over the next few years.<sup>22</sup>

### **There are clear gaps in consumer protection for BNPL users**

Our review of BNPL products has identified significant consumer protection gaps within these products. Most BNPL products do not afford consumers the same levels of protection they receive using other payment or credit methods. This can mean consumers have no access to recourse even though their functionality can look very similar to the consumer.

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<sup>19</sup> Which? (2020). PayPal to launch buy now, pay later scheme: how does it compare with Clearpay, Klarna and Laybuy? Available at: <https://www.which.co.uk/news/2020/10/paypal-to-launch-buy-now-pay-later-scheme-how-does-it-compare-to-klarna-laybuy-and-clearpay/>

<sup>20</sup> Shoosmiths (2020). Buy now, pay later services: the regulation debate. Available at: <https://www.lawcareers.net/Explore/CommercialQuestion/Shoosmiths-Buy-now-pay-later-services-the-regulation-debate>

<sup>21</sup> Which? survey of 2001 UK adults, conducted between 13th-15th October

<sup>22</sup> Finder (2020) Buy now, pay later statistics. Available at: <https://www.finder.com/uk/buy-now-pay-later-statistics>

This is true even if consumers use a credit card to pay their BNPL instalments. This is because section 75 rules don't apply if a person does not buy the product directly from the retailer. As you are using a third-party service when buying through a BNPL service like Klarna, consumers will not have section 75 protection even if they used a credit card to pay Klarna for the item.<sup>23</sup>

While each BNPL provider has a buyer protection policy,<sup>24</sup> more needs to be done to assess whether BNPL firms are treating consumers fairly if things go wrong. Which? has already heard from consumers who have struggled with obtaining a refund after something went wrong with their purchase.<sup>25</sup> Online complaints service Resolver says it has received 15,950 complaints about BNPL credit in less than two years.<sup>26</sup>

We are also concerned about the lack of clarity on a consumers' ability to raise issues to the Financial Ombudsman Service (FOS). The FOS plays an important role for consumers by resolving complaints related to most financial services. We are concerned that not all BNPL products are within the remit of the Financial Ombudsman Service. For example, Clearpay is listed on the FCA register as falling outside of the FOS' oversight.<sup>27</sup> This limits the ability of consumers to have their complaint resolved if something goes wrong while using a BNPL service.

If the FCA is to regulate the BNPL market it needs to urgently seek to ensure that the necessary consumer protections are established.

### Consumer Protection Case Studies:

#### Open-ended Survey Responses<sup>28</sup>

"It has made my life hell. I made an order for kids' clothes using Klarna June of this year, I returned a lot of items in store in June and it has been a mess ever since. The employee refunded me part of the money by mistake, and four months later I've been back and forth with Klarna and JD Sports over money owed. This has been very stressful and time-consuming. It has still not been sorted by either."

Female, aged 33, working part-time

"I ended up returning the products and not getting a refund! Took me 3 months to sort out with KLARNA very bad service will not use again."

Female, aged 30, working part-time

#### Social media comments<sup>29</sup>

"@JDSports Can you please process a refund for me as clearpay are trying to charge me for items I don't have and returned to you a week ago!"

<sup>23</sup> Money Saving Expert (2020). What is buy now, pay later? Available at: <https://www.moneysavingexpert.com/loans/buy-now-pay-later/>

<sup>24</sup> Which? (2020) From Klarna to Clearpay: your rights and tips on how to use "buy now, pay later" safely. Available at: <https://www.which.co.uk/news/2020/01/from-klarna-to-clearpay-your-rights-and-tips-on-how-to-use-buy-now-pay-later-safely/>

<sup>25</sup> Which? (2020) 'Buy now, pay later' returns nightmares: how to get your money back/ Available at: <https://www.which.co.uk/news/2020/11/buy-now-pay-later-returns-nightmares-how-to-get-your-money-back/>

<sup>26</sup> Resolver (2020) Alex's blog: will you buy now and pay for it later? Available at: <https://news.resolver.co.uk/alexs-blog-will-you-buy-now-and-pay-for-it-later/>

<sup>27</sup> FCA Register (2020) Clearpay Financial Services Limited. Available at: <https://register.fca.org.uk/s/firm?id=0010X00004J8CmDQAV>

<sup>28</sup> Open-ended survey comments from a Which? survey of 2001 UK adults, conducted between 13th-15th October 2020.

<sup>29</sup> Social media case studies gathered as part of a social media listening exercise on Buy Now, Pay Later

“@Clearpay\_UK I've paid an installment for another Asos order which didn't arrive (this is happening a lot!) Asos are unable to sort this out so how do I get a refund?”

“@marksandspencer You sent the wrong item in my order. I can't exchange it (used Clearpay) so I need to return for a refund, to then order the item I should have received & either pay post or drive to collect (nearest store is an hour round trip). Not really fair when it's your mistake.”

“@Clearpay\_UK my account says I owe but I've returned the items, do I need to pay?”

### **The impact of Covid and the FCA's response**

In relation to the FCA's temporary guidance for consumer credit we have supported the principle that temporary difficulties should not be marked permanently on credit files. While this has been in the context of the coronavirus crisis, we believe it is worth considering its application in a post-Covid world. An impaired credit status can have long term negative consequences for consumers in terms of where they access credit and the price they have to pay for it.

Similarly, a disjointed credit system will have an impact upon lenders making accurate affordability decisions. We have outlined some concerns with the BNPL market above. The lack of clarity about whether a credit check is carried out at all in relation to those products is a potential weakness in the system, and the ambiguity on whether a consumer has a debt to pay having used BNPL is a structural flaw in the current regime.

Open banking is intended to empower consumers to have ownership over their data, as well as providing lenders with a more accurate and up to date picture of a consumer's finances. Credit Reference Agency (CRA) reporting however does not provide consumers with the same level of control over their data, and it can have a disproportionate negative effect as it does not take into account wider circumstances, such as consumer engagement with creditors and any commitment to make debt repayments. The FCA has an opportunity to address potential unfair outcomes through steps to minimise the harm CRA reporting can cause consumers facing financial difficulties. Oversight of open banking firms is also vital as customer data is playing an increasingly important role in the financial services market, with potentially detrimental outcomes for consumers. Which? has already raised concerns with the FCA about the excessive use of data for pricing by insurance companies being inappropriate.<sup>30</sup> The more financial service offerings rely on the sharing of consumer data, the greater role the regulator will have to play in regulating the use of data by financial firms.

We have previously raised concerns about the need for forbearance complaints to be resolved quickly to prevent unnecessary hardship, and have provided the FCA with examples where consumers have suffered financially as a result of delays. We have asked the FCA to consult on a temporary amendment to its rules so that complaints relating to forbearance are resolved quicker than 8 weeks, in light of issues with lender capacity. However there is merit in

<sup>30</sup> Which? (2019). Consultation response to FCA General Insurance Pricing Practices interim market study. Available at: <https://www.which.co.uk/policy/money/4990/consultation-responses-insurance>

considering this solution more permanently, given the significant risk of harm arising from such complaints, as it will ensure that those who are vulnerable are swiftly and appropriately dealt with.

### **About Which?**

Which? is the UK's consumer champion, here to make life simpler, fairer and safer for everyone. Our research gets to the heart of consumer issues, our advice is impartial, and our rigorous product tests lead to expert recommendations. We're the independent consumer voice that influences politicians and lawmakers, investigates, holds businesses to account and makes change happen. As an organisation we're not for profit and all for making consumers more powerful.

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**November2020**