

Fintech Focus: Buy Now, Pay Later: A Roadmap for Providers as Regulators Continue to Increase Scrutiny

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Point-of-sale financing arrangements payable in four or fewer interest-free installments, known as buy now, pay later (BNPL) arrangements, have soared since their initial breakthrough during the pandemic.^[1] Unlike conventional point-of-sale loans, BNPL payment arrangements such as these are not subject to certain traditional consumer financial protection regulations.^[2] Accordingly, first movers—typically Fintech ventures—adhered to the BNPL installment structure despite lower profit ceilings than standard loans. Now, as consumer adoption continues to increase, some banks have begun to offer BNPL products, despite their potential aversion to the entrenchment of credit offerings that are less profitable than loans.

As BNPL has grown, regulatory scrutiny—and promises of corresponding regulation—have increased in kind. The Consumer Financial Protection Bureau (CFPB), the Office of the Comptroller of the Currency (OCC), and the Federal Reserve Bank of New York have all recently opined on BNPL and its potential impacts on consumers.^[3] This article assesses the most likely areas of focus for BNPL regulators as the industry continues to grow and provides guidance to BNPL providers in light of this dynamic regulatory landscape.

The Recent Evolution of BNPL

BNPL products are short-term financing arrangements for sales purchases, generally without interest and payable in four or fewer installments.^[4] Rather than earn money from interest like providers of traditional loans or credit cards, BNPL providers typically receive a portion of the sale price from the merchant, who in turn benefits from an increased likelihood of sale.^[5] BNPL providers traditionally forged relationships with individual merchants, offering BNPL plans at the point of purchase. But as BNPL becomes more ubiquitous, providers have begun offering pre-approved BNPL plans directly to consumers, as well as mobile applications offering BNPL plans at various merchants.^[6]

What Are the Legal Risks?

Regulators have identified several areas where BNPL plans could pose risks to consumers and providers: (i) initial credit disclosures; (ii) compulsory use of autopay; (iii) dispute resolution; (iv) consumer risk management; and (v) data harvesting and monetization. The CFPB and OCC have focused on these areas for potential future regulation.^[7]

i. Initial Credit Disclosures

The CFPB and the OCC both have criticized what they see as a lack of clear, standardized disclosure language across BNPL products.^[8] As of 2022, most BNPL products did not provide the standard cost-of-credit disclosures required under the Truth in Lending Act (TILA),^[9] because TILA does not apply to interest-free financing arrangements payable in four or fewer installments.^[10]

While BNPL products are not currently subject to disclosure regulation, the CFPB has suggested that this may change.^[11] At least one major BNPL provider is facing a shareholder lawsuit alleging, in part, that inadequate disclosures had subjected it to a “heightened risk of regulatory scrutiny and enforcement action.”^[12] Bolstering cost-of-credit disclosures as a prophylactic measure may help to stave off such scrutiny, though the best form and content of such disclosures will depend on the circumstances.

ii. Compulsory Use of Autopay

The CFPB has reported that most BNPL providers require consumers to use autopay for their repayments. Moreover, according to the CFPB, some BNPL products make it challenging to revoke autopay.^[13] In other credit contexts, the CFPB has banned the use of autopay for consumer loan payments.^[14] BNPL providers may be well advised to limit exclusive reliance on autopay features for their payment plans where possible.

iii. Dispute Resolution

Inadequate dispute resolution is the most common source of BNPL-related complaints in the CFPB’s Consumer Complaint Database.^[15] Merchant returns and disputes, for example, may be difficult to coordinate with BNPL providers that were not directly involved in the sale.^[16] Consumers have reported auto-repayments continuing despite an ongoing dispute, as well as difficulties informing BNPL providers of disputes.^[17] In other loan contexts, such as open-ended credit deals or credit card issuances, such practices could potentially run afoul of dispute-resolution regulations in Reg. Z.^[18] While BNPL products do not currently face such regulations, BNPL providers would be well served by ensuring clear, streamlined, and coordinated processes for handling merchandise returns and disputes.

iv. Consumer Risk Management

The CFPB, OCC, and the Federal Reserve Bank of New York have all stressed their views that BNPL products pose financial risks to consumers.^[19] For example, the OCC has commented that the ease of access and high approval rates for BNPL products can lead to consumers overextending.^[20] Similarly the CFPB has warned of “loan stacking,” where a consumer takes on BNPL financing arrangements from several providers at once, increasing their risk of default.^[21]

Regulators have argued that these risks stem, in part, from insufficient credit reporting from BNPL providers. BNPL providers often do not provide real-time data on their consumers’ debts, meaning competitors cannot assess the risk of loan stacking.^[22] Accordingly, the OCC has advocated for comprehensive information-sharing requirements for the BNPL industry, pointing to disclosure requirements imposed on creditors covered under the Fair Credit Reporting Act (FCRA).^[23]

On the other hand, even where information on BNPL customers is available, BNPL providers often perform credit checks that do not reach all available information. The OCC has cautioned banks to implement vetting procedures for BNPL lending, including by establishing underwriting criteria, credit-loss allowance considerations, and methodologies to assess repayment capacity, fees, and likelihood of charge-offs.^[24] Many of these procedures can be implemented by incorporating BNPL products into a bank’s existing methodologies. However, the OCC notes that some banks charge off loans on a fixed delinquency timeline, such as 120 or 180 days past due, which may be too long to capture the short-term BNPL products.^[25]

v. Data Harvesting and Monetization

The CFPB has repeatedly expressed concerns over data privacy in the BNPL industry,^[26] and has asserted its intention to introduce regulation protecting personal financial-data rights.^[27] BNPL users tend to use BNPL credit products repeatedly;^[28] accordingly, BNPL providers generally have access to extensive consumer shopping, demographic, and financial data. The data gathered will only grow as BNPL products are increasingly offered through mobile applications.^[29] BNPL providers should ensure that their usage of consumers’ data comports with their initial disclosures and all applicable data privacy laws.

Conclusion

Given the increasing prevalence of BNPL in the financial lives of consumers, it is critical for BNPL providers to track and, where possible, anticipate regulatory concerns and requirements. Through such care, BNPL can remain a valuable tool for consumers to avoid interest and for providers and their partners to drive demand.

Footnotes

[1] <https://www.fisglobal.com/en/about-us/media-room/press-release/2022/global-e-commerce-market-projected-to-grow-55-percent-by-2025-fis-study-finds> ; <https://libertystreeteconomics.newyorkfed.org/2024/02/how-and-why-do-consumers-use-buy-now-pay-later/>

[2] 15 U.S.C. § 1026.1(c)(1)(iii).

[3] *E.g.*, https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf; https://files.consumerfinance.gov/f/documents/cfpb_convergence-payments-commerce-implications-consumers_report_2022-08.pdf; <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn10>

[4] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn10>

[5] <https://www.thisweekinfintech.com/the-biggest-winner-of-bnpl-is-mastercard/?ref=the-main-edition-newsletter>

[6] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[7] https://files.consumerfinance.gov/f/documents/cfpb_convergence-payments-commerce-implications-consumers_report_2022-08.pdf

[8] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn10>;
https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[9] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[10] 15 U.S.C. § 1026.1(c)(1)(iii).

[11] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[12] *Kusnier v. Affirm Holdings, Inc.*, (N.D. Cal., Dec. 8, 2022), Case No. 3:22-cv-07770.

[13] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[14] *See* 15 U.S.C. § 1693 et seq. (Electronic Funds Transfer Act), as implemented by Regulation E, 12 C.F.R. § 1005.10(e)(1).

[15] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[16] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn10>

[17] *Id.*

[18] *See* 15 U.S.C. § 1601 et seq. (TILA), as implemented by Regulation Z, 12 C.F.R. § 1026.12(c), 12 C.F.R. § 1026.13;
https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf.

[19] https://www.consumerfinancemonitor.com/wp-content/uploads/sites/14/2024/02/ABA-Risk-and-Compliance-Buy-Now-Pay-Later-DMFIRM_4113087651-002.pdf; https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf; <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn14>

[20] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn14>

[21] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[22] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

[23] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn14>

[24] <https://www.occ.gov/news-issuances/bulletins/2023/bulletin-2023-37.html#ftn10>

[25] *Id.*

[26] https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf ; https://files.consumerfinance.gov/f/documents/cfpb_convergence-payments-commerce-implications-consumers_report_2022-08.pdf

[27] https://files.consumerfinance.gov/f/documents/cfpb_convergence-payments-commerce-implications-consumers_report_2022-08.pdf

[28] <https://libertystreeteconomics.newyorkfed.org/2024/02/how-and-why-do-consumers-use-buy-now-pay-later/>

[29] https://files.consumerfinance.gov/f/documents/cfpb_convergence-payments-commerce-implications-consumers_report_2022-08.pdf ; https://files.consumerfinance.gov/f/documents/cfpb_buy-now-pay-later-market-trends-consumer-impacts_report_2022-09.pdf

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