


# The Messenger Business.

It's time to break the news.

[News](#) [Politics](#) [Opinion](#) [Business](#) [Entertainment](#) [Sports](#) [Tech](#)

 **TRENDING NOW** | Americans Warned About Traveling to Multiple Caribbean Hotspots Ahead of Carnival, Spring Break

## Why Buy Now, Pay Later Is the 'Phantom' Debt

Are these interest-free short-term loans too good to be true?

Published 12/21/23 02:28 PM ET | Updated 01/05/24 03:56 PM ET

[Kathleen Howley](#)



---

**S**preading out the cost of a purchase without accruing interest may seem like a no-brainer, especially during a [holiday shopping season](#) when credit card rates are at record highs and prices just get higher and higher.

With a few taps at many online and even in-store checkouts, shoppers use so-called buy now, pay later (BNPL) providers like Affirm, Klarna, Afterpay, and PayPal to seemingly get the best of both worlds — delay paying in full but also avoid any finance charges, if the loan is short enough. For better or for worse, they also escape the radar of traditional lenders and [credit scorers](#), at least for now.

But those same features also mean the hottest new credit product — which is becoming more mainstream by the second — could tempt people to overspend and take on more debt than they can handle. And while interest isn't an issue, late fees can stack up quickly when payments are due every two weeks, adding up to as much as 25% of the purchase price under some plans.

“If you use it well, it can be helpful, but if you are careless, it can get you in trouble,” said Rod Griffin, senior director of public education and advocacy for the credit bureau Experian. “It’s very tempting when you’re buying presents, but the bills are going to come due fast.”

Perhaps most worrisome, though, are the hidden pitfalls for both consumers and the financial system. This type of loan is so new that it isn't yet captured by credit scoring systems or in many cases reported to the major credit bureaus, Griffin said. That means lenders don't have the full picture of the risks each borrower is taking on. And that could make it easier for borrowers to get in over their heads and tough for policymakers to measure or regulate the industry.

“Until there is a definitive measure for it, there is no way to know when this [phantom debt](#) could create substantial problems for the consumer and the broader economy,” Wells Fargo economists Tim Quinlan and Shannon Seery Grein wrote in research earlier this month.

On the one hand, BNPL could be a “lifeline” for households that are strapped for cash or having a hard time getting traditional credit, they wrote. But it could also be an “unregulated danger zone that could lull consumers into a false security in which many small payments add up to one big problem.”

---

## Read More

[Buy now, pay later payment plans are fueling a consumer debt boom and raising concerns about customer data](#)

---

[Colorado Business Pays \\$23,000 Debt in Loose Coins: 'A Symbolic Middle Finger'](#)

---



[SWAT Team Destroys Man's Business While Looking For Suspect – Why Won't City Pay For It?](#)

---

[America Is Now Paying More in Interest Than It Does for Defense](#)

---

[China's mortgage boycotts: Why hundreds of thousands of people are saying they won't pay](#)

---

[Yellen: Debt Limit Deadline Now June 5](#)

---

Although the explosive interest in BNPL warrants more scrutiny, the risk appears to be manageable so far, the economists said. Even though estimates show the number of BNPL loans surged more than tenfold between 2019 and 2021, pushing the dollar volume from [\\$2 billion to \\$24.2 billion](#), that's still only about 2.5% of the size of the credit card market, they said.

In its most basic form, BNPL is a modern type of layaway, except that the shopper gets their jewelry or toy right away and the payment platforms are integrated right into the checkout system.

In order to split their purchase into four equal payments, shoppers — often from younger, more tech-savvy generations — choose a BNPL platform from the various payment options at checkout, making the first payment immediately and then agreeing to three more over six weeks.

Most pay with their checking account (usually through a debit card) but they can also use a credit card. Eligibility is determined in minutes by a “soft” credit check that doesn't impact their credit score.



Buy Now, Pay Later loans are exploding in popularity, but they aren't yet captured by credit scoring systems or even reported to the major credit bureaus in many cases. sefa ozel/Getty Images

A downside, though, is that each purchase creates a new loan (averaging \$135) with its own repayment schedule. So if someone misses a payment and/or overdraws their bank account to pay it, late fees or overdraft charges can pile up, said Adam Rust, director of financial services at the Consumer Federation of America.

“If you are stacking loans, it increases the chance that you will miss the payments that are due for each,” Rust said. “If you’re paying for multiple items, and sometimes with multiple BNPL companies, it can get confusing.”

Plus, consumer advocates and regulators argue, anyone who makes their BNPL payment with a credit card isn’t escaping interest charges if they end up carrying a balance on that card. They also leave themselves vulnerable to late fees on two products rather than one — unless their provider doesn’t charge them (like [Affirm](#) and [PayPal](#).)



Wells Fargo’s Quinlan and Grein said BNPL could become the “phantom menace” because there’s no consistent central monitor to measure the industry or its effect on borrowers and lenders.

In the last two years, Experian and the two other major credit bureaus announced plans to accept BNPL payment data, but [each bureau’s plan is different](#) and some BNPL companies have resisted providing the data, [instead touting](#) that using their products protects people’s credit scores.

Without a standardized approach, even nailing down the status of this shift is difficult. It’s unclear whether and how much data is reported to the bureaus, but also how and when it gets incorporated into credit scores.

Without both, any lender runs the risk of extending credit blindly, the Office of the Comptroller of the Currency warned earlier this month in a bulletin it issued to banks.

“Existing credit scoring systems are not designed to capture the very short-term nature and structure of BNPL loans. Incomplete reporting of BNPL loans could make it difficult for lenders to know the total dollar amount of debts and other obligations that applicants have before determining whether to approve them for new credit,” [the OCC wrote in the bulletin](#). “It could take some time before BNPL activity is consistently reflected in credit scores.”

Experian’s Griffin estimated the process could take another year.

“We are not yet sure how it will be incorporated, but it should be fairly soon — within the next year,” he said.

Meanwhile, a four-payment interest-free BNPL plan has become particularly appealing with inflation so high and the average interest rate on a [credit card topping 21%](#), a record high for the almost 30 years that the Federal Reserve has been tracking it.



On Cyber Monday — the post-Thanksgiving holiday shopping day promoted by online retailers — BNPL usage [hit an all-time high](#), contributing \$940 million, or 7.6%, of the \$12.4 billion in online spending that day, according to data from Adobe Analytics. That's 42.5% more than BNPL contributed last Cyber Monday, the group said on Nov. 28, forecasting November to be the biggest BNPL month on record.

But if other options emerging from BNPL providers are any indication, it's not just the lack of interest charges that people find so appealing about BNPL. For shoppers who want to borrow for say, six or 12 months, many providers now offer an alternate choice at checkout that more closely resembles an installment loan. These may charge interest as high as 36% in some cases.

Indeed, surveys show customers like the ease and simplicity of BNPL. Among BNPL customers surveyed by the Federal Reserve Bank of Philadelphia in November 2021, convenience was the most commonly cited reason for using BNPL. Almost 53% cited it, compared to just 24% who said the lower cost was a factor.

BNPL emerged first as an online option, becoming a fixture at giants like Amazon and Best Buy, but it has been pushing into physical stores.

Customers can now make payments on phone apps, applying ahead of time to get a barcode they can use in stores. And just this week Walmart said Affirm, already available at Walmart.com, would be added to self-serve kiosks at [over 4,500 Walmart stores](#) around the country.

The Consumer Financial Protection Bureau opened an inquiry into BNPL in December 2021, citing concerns about the impact on borrowers. The regulator has since pledged to ensure BNPL providers [offer the same protections](#) and submit to the same examinations as credit card companies.

"It's the ease of using it that is so tempting," said Experian's Griffin. "If you use this kind of resource to deliver the gifts everyone wants for holidays, the bills are going to come due fast, and it's possible the new year won't be so happy."



---

**Read next** [Woman Pleads Guilty to DUI After Crashing Into DUI Warning Sign. Cops at DUI Checkpoint Came to Rescue](#)

---