



Advertising Compliance: Getting Ready for the Banking Examination

Jonathan Foxx *

Advertising is often central to a loan originator's marketing plans. After all, if prospective borrowers can't even find you when they need mortgage loans, there's nothing left but word of mouth, dropping off bagels at real estate brokers, giving away pens and pads with your name on it, offering occasional, educational and promotional presentations on loan products, and hanging out a website shingle with the hopes that you will be listed on Page 10 of Google Search.

Informing the public of loan products is a highly regulated activity in mortgage banking and finance. Buzz words, restricted words and phrases, and trigger terms can be a nasty nest of vipers that will catch you up in a regulator's net. The regulatory areas involving mortgage banking advertising include the Fair Housing Act, Equal Credit Opportunity Act (ECOA), Truth in Lending Act (TILA), Federal Trade Commission's Mortgage Advertising Rules, FHA mandates, Real Estate Settlement Procedures Act (RESPA), Unfair, Deceptive, or Abusive Acts or Practices (UDAAP), fair lending, the SAFE Act, the Fair Credit Reporting Act (FCRA), and state regulations. Clearly, advertising compliance is complex!

My firm looks at thousands of potential advertisements a year that are sent to us by our clients for clearance. Although we provide them with our Advertising Manual, which is deep and broad in application and contains many forms and formats, each advertisement still often needs a review, especially at the commencement of a marketing campaign. Our clients want to comply with federal and/or state advertising regulations; however, they feel continually constrained as to how best to both stay within bounds of regulatory compliance and also create appealing advertisements. Of course, banking examiners

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don't much care about how engaging and captivating an advertisement is; these professionals are tasked with protecting the consumer in accordance with required regulatory guidelines.

One of the very first requests a regulator asks at the outset of an examination is to receive for audit all advertisements involving contact with the public during the scope period. Woe be unto the company that does not have each and every advertisement ready and available for audit! And woe be unto the company that lets a regulator somehow uncover an advertisement that was not disclosed at the time of an examination – even if the advertisement had no violations in it, the trust factor with the auditor will not be easily re-established!

As many of you know, Lenders Compliance Group's orientation is what I call "applied compliance" – not the theoretical approach to compliance that seems to work in theory, but often becomes controversial in the on-going implementation of regulatory compliance. In this article, I am going to provide a practical approach to guiding you through the maze of certain advertising compliance rules as well as regulatory expectations. Obviously, the article is not meant to be comprehensive. But it is aimed at providing suggested ways and means toward the kind of hands-on, applied compliance that my firm handles every single day on behalf of our clients.

This is a two-part article. In this first part, I will discuss some basics, give you the principal ways to prepare for advertising compliance examinations, and highlight the banking examiner's expectations. In the second part, we'll explore marketing campaign development, the use of advertising checklists, triggering terms (the advertised words or phrases that "trigger" the need for additional disclosures), and the way advertisements impact fair lending.

BASICS

First and foremost, let's be clear about what is a viable advertisement.

There are essentially two features that are foundational: 1) it must be truthful; and 2) the intended audience must be "reasonably capable" of understanding the information contained in it. The advertiser's intent is not the sole determining compliance factor; rather, the manner in which the advertisement actually is received by the audience is dispositive. What is reasonable? One of my colleagues often refers to the "reasonable person rule" as the "village idiot rule;" that is, if the village idiot can be expected to understand the message, the "reasonable person rule" test may be passed. Sounds about right! In effect, a representation, omission, or practice is material if it is likely to affect a consumer's choice of or conduct regarding a product or service.

Put it this way: the general test is whether the "average" person in the intended audience – persons expected to read or hear the advertisement and to be influenced by it – will understand the message clearly. Perhaps it is not possible to quantify the number of persons in the intended audience who need

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to understand the advertisement clearly, but it should be understandable by a substantial number in the audience.

It is not necessary for an advertisement to state every feature of the loan product: an advertisement is not a legal treatise. That said, any features and any terms (including prices) or any potential benefits should be presented in a manner that does not mislead. That means no false impressions caused by omissions. Advertising is a sinkhole of omissions, whether intentionally caused or the result of an error.

For the most part, the American Bankers Association's definition of an advertisement offers a concise understanding,¹ as follows:

“Advertisement” means any message paid for by the sponsoring institution in a newspaper or magazine, on radio or television, on billboards, or in the form of brochures, statement stuffers, direct mail, and other printed material, including applications. Signage, either interior or exterior, and displays also are included. Although not strictly advertising, the terms also embrace oral communications between [bank] employees and actual or potential customers, including telephonic and face-to-face solicitations and inquiries.”

Added to the foregoing definition would be social media advertising and website advertising - in fact any contact with the public where the goal of the message (written or spoken) causes or can be expected to cause an “intelligent purchase decision” by a consumer who sees or hears the advertisement and, being influenced by the information contained therein, can decide that using the advertised product or service is in his or her best interest - irrespective of whether the product or service is obtained from the advertiser. However, advertising does not include direct personal contacts relating to the negotiation of a specific transaction, or informational material distributed to only business entities.

GETTING READY FOR THE BANKING EXAMINATION

There are five aspects involving preparation for advertising compliance. If any one of these is not ready for and responsive to the regulator's document requests, the company will be scored down, and even may lead to administrative actions on the part of the supervising agency. Let us take a tour of these five components to advertising compliance, as well as the actions you should be taking in advance of an examination.

1. **MEDIA.** Determine the types of advertising media used and types of services or products that have been promoted. Be sure to review, update where needed, and test the relevant processes for:
 - a. Advertising Policies and Procedures
 - b. Advertising Files and Folders
 - c. Advertising Expense Records (viz., particularly payments to various media, such as radio, television, and newspapers)
 - d. Telephone solicitation and radio and television commercial scripts

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- e. Social Media Interactions
 - f. Website URLs
2. COMPLIANCE TRAINING. Determine the extent, adequacy, fulfillment, and scope of the compliance training received by staff responsible for responding to consumer inquiries and providing loan product and service information. In my opinion, all employees should take such training.
 3. TRAINING-TELEPHONIC AND ELECTRONIC COMMUNICATIONS: Determine the extent, adequacy, fulfillment, and scope of compliance training given to staff engaged in phone, email, and any electronic solicitations for loan products and services.
 4. REVIEWS: Determine the extent, adequacy, fulfillment, and scope of the reviews conducted on advertising and public notices for compliance with all applicable rules and regulations.
 5. AUDIT PROCEDURES: Determine the existing and needed audit procedures involving all advertising and solicitations (written or spoken) in order to comply with applicable regulatory requirements. Include in the audit procedures a means by which monitoring can be functionally implemented, such as the monitoring of outbound calls to consumers to ensure compliance with applicable law and internal policies; ensuring compliance with legal obligations; and regularly evaluating employee and service provider (viz., Marketing Services Agreements) or affiliate entities performance (if applicable).

During the examination, the regulator will be testing for advertising compliance. So you should not wait until the time of a banking exam for you to test your advertising compliance. We recommend a review, at least quarterly, of your advertising files. Consider taking these actions:

1. Review your advertising since the previous examination. If the file is voluminous, select a sampling of advertisements. A typical sample selection should include these reviews:
 - a. Product and service type
 - b. Media used (television, newspaper, radio, electronic, and so forth)
2. Determine if the reviews include a way – such as via checklists – for gauging compliance with applicable regulatory requirements. Assess the effectiveness of the compliance review procedures based upon a sampling of the advertising file.
3. Rate the advertisement for compliance with regulatory mandates, using (“1”) for fully compliant and (“5”) for least compliant. Specify, test for, and document all correction actions.
4. Maintain the documents involving the periodic review. Include in the review any complaints associated with the advertisement and the resolution of such complaints.

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EXAMINER'S AUDIT CRITERIA

When developing advertisements and market campaigns, differing regulatory frameworks may be involved and interlocked. For instance, in Regulation Z (TILA) an advertisement is a commercial message in any medium. For purposes of the FTC's Mortgage Acts and Practices Rule (MAP Ad Rule),² a commercial communication is a statement designed to effect a sale or create an interest in purchasing goods or services appearing in various formats, including the Internet or any other medium.

Examiners will evaluate the advertising materials and disclosures across all media, including print, television, radio, telephone solicitation scripts, and electronic media including the Internet, email and text messages. If the company engages in telemarketing, examiners are going to listen to a selection of the sales calls. Furthermore, if the company uses a third-party lead generator, there will be a deep dive into the extent and scope of any such relationships, in addition to a review of affiliated or other service providers (i.e., as a broker or agent) to advertise, offer, or provide loans or other products and services.

Anticipating the examiner's audit criteria is critical to a successful review.

Typically, a regulator will determine whether advertisements and promotional materials for mortgage loan products contain material misrepresentations,³ expressly or by implication, of the following:⁴

- the existence, nature, or amount of fees or other costs;
- number, amount, or timing of payments, including whether the payment includes amounts for monthly escrow payments for taxes and insurance;
- credit qualifications for a particular product or program;
- potential for default;
- product type;
- product effectiveness with respect to debt elimination;
- nature of counseling services; or
- the existence, nature, or amount of prepayment penalties.

There are red flags that examiner's look for when evaluating advertisements, such as the use of fine print, separate statements or inconspicuous disclosures. They will want to know if additional products or services are sold or offered in connection with the loan, such as credit insurance products, home warranties, or annuities. Additionally, the regulator will determine whether advertisements and promotional materials provide timely, clear, and understandable information about the existence of costs, payment terms, penalties, or other terms and charges, the reasons for their imposition, and the salesperson's compensation from cross-sales.

The audience for the advertisement is factored into the overall compliance evaluation. An examiner will determine the target audience for each type of advertisement for a product and service as well as whether

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the company designs and publishes advertisements, promotional materials, disclosures and scripts that are “comprehensible by the target audience.”

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¹ Statement of Principles on Financial Advertising, American Bankers Association

² Mortgage Acts and Practices-Advertising, Final rule, 16 CFR Part 321, Federal Trade Commission, FR/76-41, July 22, 2011, Rules and Regulations

³ See also the MAP Rule, 12 CFR 1014.3, which applies to nonbanks and certain state-chartered credit unions, which lists nineteen examples of specific prohibited claims.

⁴ See Module 2 of the CFPB’s Examination Procedures (Mortgage Originations), January 2014

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