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Compliance & Social Commerce

Tweets & Posts



Social media represent a relatively new Internet-based phenomenon, having existed for only a dozen years and enjoyed wide popularity for about five. But they have become such staples of our culture that they will likely be a permanent part of online commerce, in some evolving fashion, and this commerce will increasingly include financial services.

Social media or, more specifically, “social commerce” sites include social networking sites, such as Facebook, MySpace, and LinkedIn; sites where consumers exchange information about products and services, such as ratings and reviews forums on company order pages; and company-sponsored blogs.

Consumers have long discussed products and services with each other and have asked and received advice about what to buy. But the social networking tools available to the purchaser of financial services today are unprecedented, and nearly all have evolved over the last decade.

Who participates in social commerce? It’s not just mil-

SOCIAL NETWORKING TIMELINE

The term “weblogging” (now shortened to “blogging”) is coined to describe the practice of keeping an online diary for others to read. The first public social networking site (sixdegrees.com, now defunct) was launched.

1997

1998

1999

2000

2001

2002

& Blogs



lennials (i.e., adults born after 1977). For example, in 2008 the fastest-growing Facebook demographic was adults over age 50. According to a study published in 2008, 75 percent of online adults in the United States participate in social content at least once per month, including using traditional social networking sites like MySpace and LinkedIn as well as companies' own Web sites that publish ratings and reviews. More than one-third of online adults post ratings or reviews of products and one-third actively participate in blogs. The amount of time users spend on social media sites is growing, too. In 2008, the time spent on membership sites (e.g., MySpace, LinkedIn, Facebook) increased by 63 percent over 2007.

The growth of social commerce Web sites as communication channels for discussing products and services is too significant for bank marketing officers to ignore. Financial institutions will have to embrace new and emerging com-

munication methods to stay relevant and to communicate with customers and prospective customers in forums where they are most likely to be reached.

Banks use social networking sites for many different communication and marketing activities, but typical "command and control" advertising is not the goal of most social commerce forums. One of the differences offered by social commerce sites is the ability to cultivate the bank's brand and facilitate trust in the marketplace. A July 2009 J.D. Power study indicated that 36 percent of consumers are driven to select a financial institution based on brand image; social commerce communication is perfect for building brand image. A review of a sample of banks' social networking sites, primarily on MySpace, Facebook, and Twitter, indicates that these sites are used for

- promoting financial products and services to customers and prospects

LinkedIn and MySpace launched.

Facebook launched (open only to college community).

YouTube launched; the term "social commerce" is coined to describe the sharing of views about a product or service with other consumers.

Twitter launched; Facebook is made open to everyone.

Facebook becomes the largest social networking site in the United States, with 250 million registered users; Twitter grows 752 percent.

Twitter grows by 50 percent per month; at least 100 financial institutions have Twitter accounts and more than 500 have Facebook pages.

2003

2004

2005

2006

2007

2008

2009

- maintaining a forum for customers to rate and review products and relate anecdotal experiences with the institution related to products or services
- providing information on bank promotions, contests, community activities, and the like
- responding to questions and customer service inquiries
- offering a venue for customer complaints

A review of 15 bank Facebook pages found that banks not only educate the public about their products and services but also hold contests, promote bank-sponsored events including charity fundraisers, and provide general community-related information. Some of the pages reviewed have several hundred followers or “fans,” so it appears that social networking sites can be an effective public relations and marketing tool.

However, engaging in social commerce activities raises some unique regulatory issues that compliance officers cannot ignore and some ethical issues that should be addressed.

The regulatory compliance issues surrounding social networking activities of financial institutions fall into five categories:

- advertising regulations
- fair lending/CRA compliance
- records compliance
- information security
- BSA/AML regulations and Reg. E

This article provides a perspective on the types of issues that should be reviewed by compliance officers when managing the risks of using social networking as a customer service tool. As with any new compliance challenge, compliance officers will need to determine their institutions’ specific risk, establish review and monitoring procedures, and determine how to use the customer information to bolster their banks’ compliance efforts.

Advertising Compliance

Typical social networking commercial sites aimed at consumers, such as Facebook and MySpace, are perfect for communicating to consumers about bank products. A random sample of bank pages viewed during the last 30 days found that in their posts institutions mention all types of financial products, stream video commercials, and post product brochures. Also noted: lots of compliance errors.

For regulatory purposes, banks’ messages on social commerce sites generally fall into the category of advertisements. Whether messages from consumers are considered “advertisements” is a complex question. Because the bank ultimately controls the site and should remove information that is incorrect, a reasonable view would be that any communication that clears the bank’s review and remains visible to the public does qualify as an advertisement for regulatory purposes. What regulations should the compliance officer consider?

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Regulation Z Requirements for Loan Advertising

Reg. Z has a plethora of requirements that apply to advertisements of loan products. Generally, if an advertisement states specific terms, only those actually offered by the bank should be included. There are many other loan-related advertising rules in Reg. Z, including the following:

- If triggering terms are used for open-end or closed-end loans, the other requisite disclosures must also be included (in electronic ads, the other terms can be referenced by a link).
- New requirements for home loan products (effective October 2009) require more extensive disclosures if rates or payments are mentioned in the ad; HELOC advertising requirements have also been extensively rewritten.
- There are new rules regarding the use of the term “fixed” in connection with loans where the rate or payment may increase under certain circumstances, as well as new rules for advertising ARM loans.
- The 2008 changes to Reg. Z include rules regarding misrepresentations (e.g., misleading comparisons, misrepresenting government endorsements, etc.).
- Reg. Z has a host of advertising rules related to credit cards (revisions to these rules are effective in 2010) so mentioning rates—especially introductory or promotional rates—would require additional disclosures.

In a social networking environment—where the bank’s posts strive for informality and where consumers can make their own posts—making sure that all information is strictly in compliance with the advertising rules could be a challenge. Here are a couple of actual posts (with identifying information removed):

A Twitter post from July 19, 2009:

Mortgage rate update—30-year fixed 5.375% APR, 15-year fixed 4.875%, FHA 5.50%. Apply today at [web address]

A brochure posted on Facebook (found on July 15, 2009):

A Home Equity Line of Credit with NO CLOSING COSTS (6 mo. introductory rate) 3.50 APR, then as low as 4.50% APR**

The Facebook posting seems to be a reprint of an ad that appeared in a printed format. The asterisks probably referred the reader to the additional disclosures, but unfortunately those disclosures did not appear on the Facebook page. In cases where brochures are reproduced on a site, the entire document should appear.

Regulation DD Deposit Advertising

Reg. DD’s deposit advertising rules apply to information posted by the bank. For example, if the APY is stated, the other requisite disclosures must be stated. The mention of bonuses also requires additional disclosures.

The following Tweet was noted during the last week of



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June 2009:

While you're there, open a CD (up to 3% interest) or savings account.

A Facebook entry from the beginning of July 2009 offered the following:

Become a Facebook fan to get a 4% CD during the month of July.

FDIC Membership Advertising Requirements

In nearly all cases the bank should include the “Member FDIC” or similar logotype on its page or with its logo. In our review of Facebook pages and Twitter messages, this logo was absent in the majority of cases, even when deposit accounts were specifically mentioned.

Fair Housing Act

If the bank mentions a loan to be secured by the borrower’s home, the equal housing lender logo should be included, and no advertising communication can indicate illegal discrimination. This was a widespread error we noted when reviewing Facebook pages with mentions of home-related lending. In the home equity line of credit ad cited above, there was no equal housing lender logo even though the posting was a brochure.

Nondeposit Retail Investment/FINRA Advertising Restrictions

Under the nondeposit retail investment guidelines any mentions of nondeposit investments require disclosures, and such advertisements must be separate from insured deposit information.

FINRA (Financial Industry Regulatory Authority) has determined that communications on social networking sites that are open to the public are considered for regulatory purposes to be advertisements, and institutions must comply with FINRA’s applicable regulations. In addition, FINRA has stated that if an institution allows its employees to set up profiles on a social networking site that provide

work-related information, those profiles will also be considered advertising if they are open to the public. If, however, an employee’s page is open only to the employee’s own contacts, it will be considered “sales literature” and subject to applicable regulations. In any event, the institution will be responsible for compliance if it allows such practices to continue. To avoid this outcome, the institution should establish a policy regarding the posting of work-related information on employees’ personal social networking pages and will need to block such activity on work computers. The corporation’s own site should also be carefully monitored for compliance.

If the institution wants to put product information on its social networking site—or mention products at all—then FINRA’s preapproval procedures should be followed and the normal compliance requirements, such as the following, apply:

- No exaggerations can be included.
- All material facts must be disclosed.
- No forward-looking statements can be included.
- Clearly identify the b/d sound basis for evaluation.
- Mutual funds disclosures must be filed with FINRA in advance.

Sales of Insurance by Depository Institutions (GLBA)

The insurance disclosures (not FDIC-insured, not guaranteed by the bank, not guaranteed by any government agency, may lose value, etc.) should appear if the bank mentions insurance products in its posts or on its pages.

UDAP Rules

It’s worth taking a look at the regulatory agency UDAP issuances (OCC AL 2002-3; FDIC FIL 57-2002, and FIL 26-2004) as well as your state’s UDAP rules to make sure that everything said on the site is true and not deceptive in any manner. Having a system in place to monitor customer comments is imperative to ensure that a misinformed state-



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ment that is posted does not remain and thereby obtain the bank’s imprimatur.

Fair Lending/CRA Compliance

According to Reg. BB and the other CRA-related regulations, the bank is required to keep all CRA-related comments it receives in its CRA public file. Comments received through social networking sites or through a ratings and reviews page would appear to qualify. Even comments that do not meet the filtering or moderation standards or are removed from a posting page should be maintained in the public file if they qualify under the regulations. While this may seem like an unfavorable development, a bank is actually much more likely to get a favorable comment via one of these channels than a negative one. Research shows that consumers who are likely to comment or provide a rating on a product or company are much more likely to rate it favorably than not. So encouraging these social networking activities could actually increase the number of favorable CRA comments the bank receives.

Because these sites are a new, convenient channel for the voice of the consumer, there is a good chance that, in an environment that encourages robust communication among customers, there will be a complaint issued every now and then. Compliance professionals should welcome this development, insist on being part of the process, and be interested in viewing each and every one of these. Why? One of the most difficult things to achieve in a multi-branch environment is to be aware of what is actually happening in the branches. In many cases, the bank’s employees might not want customer complaints to reach the “corporate” level because such complaints may be perceived as reflecting badly on them or their operations. When information flows freely through social networking venues, the barriers of communication are broken and the compliance officer can actually hear the voice of consumers—and learn more about how the bank’s policies and practices are perceived by the public.

For example, in many cases, when a fair lending–related situation arises, the bank’s upper management and compliance staff often had no idea that a customer was unhappy or that there was a problem with a bank employee until a complaint was made to a regulatory agency. Hearing the consumer’s voice early in the process can only make a compliance officer’s job easier in the long run. If there’s a problem with a process or the bank is perceived to be acting in a way that is not consumer-friendly, learning about it early allows the bank to respond in a thoughtful way and fix the problem.

Records Management Compliance

Records management can be a challenge in the environment of social commerce. Several laws and regulations require that records be retained for specific time periods. For example, Reg. B requires that all records related to a loan application be maintained for 25 months. Thus, if a customer whose application was denied posts a complaint related to the denial, that comment would need to be retained, even if it were removed from the site. This also applies to ratings and reviews forums. Even if the review was filtered during the moderation process, the actual comment needs to be retained.

Both Reg. Z and Reg. DD require that evidence of compliance be retained for two years. If deposit or loan information on a bank’s social networking site qualifies as advertising, that electronic communication should be retained so that it can be retrieved for purposes of documenting compliance with these regulations.

FINRA has determined that communication on social commerce sites related to activities that it governs fall into its record retention rules and must be maintained for three years.

E-discovery requirements will apply to all records maintained by the bank through its social commerce forums, so if the comments and material on the bank’s social commerce sites are retained, they have to be available for discovery.

A best practice is for the bank to formulate policy to determine



what information will be retained and for what length of time. It is helpful if the comments and information are sortable by topic—that way, if sensitive comments need to be retained for a longer time period they can be identified and stored appropriately.

Information Security

One of the most important risk management issues involved with social networking sites is information security. Direct messages and posts from consumers that contain sensitive information such as account information or personally identifiable information are subject to hacking and phishing attacks, which bear a risk of fraud or identity theft; Facebook was hit by multiple phishing attempts early in 2009. It is important for financial institutions to have the capability to secure messages with sensitive information or have instant moderation of messages in order to prevent their exposure to the public.

Bank Secrecy Act/Anti-Money Laundering and Other Payment-Related Compliance Considerations

This area comes under the category of future consideration. There is serious speculation that the most popular social networking sites will eventually facilitate person-to-person (P2P) payment orders, either with real currency through banking channels and nonbanking channels such as PayPal, or through the use of their own virtual currency. To the extent that banks are involved in this activity there are certainly BSA/AML considerations surrounding these payment channels. For instance, an institution would need to incorporate this type of payment activity into its normal BSA/AML monitoring processes to determine whether the activity is high risk. Appropriate review thresholds and trending analysis would be necessary.

Also, if the bank is directly involved in facilitating payments through a social networking site, then Reg. E disclosures would be required for payments made electronically.

Other Risk-Related Issues

With the use of social networking sites, other risk management concerns arise that are not directly related to regulatory compliance. Specifically, the sharing of bank-related information on an employee's personal site poses some reputation risk to the institution. Just as most institutions have now grappled with the risks surrounding their employees' use of e-mail and the Internet on work computers, the issue of when employees can use social networking sites and how much they can say about their jobs and companies should be a subject of bank policy. Both the human resources policy and the bank's code of conduct are possible venues for this policy, but no matter where the policy resides, it should clearly address the following questions:

- **May employees access their personal sites during work hours?** For example, can an employee update his or her Facebook, MySpace, or LinkedIn site during a break or lunch, or at any other time?
- **How much work-related information will the bank allow employees to post on personal social networking sites?** Can the employee reveal the name of the bank or his or her title, job description, or similar information? Such information often appears on business-related networking sites, such as LinkedIn. Should the information shared be limited to just the bare facts of the employee's job—and no additional company information shared?
- **With whom can the employee connect on his or her site (i.e., "link with," "friend," etc.)?** The bank should consider whether its policy will address the practice of employees connecting with bank customers—unless there is a pre-existing relationship—because this is the equivalent of allowing the employee to take home (and store) the bank's proprietary customer information. There have been instances of employees leaving one institution and soliciting customers of the previous institution with whom they were connected via social networking pages.
- **Who has the authority to post information on behalf of the bank on the bank's own social networking sites?**
- **If the bank has a ratings and reviews site, may employees post their own ratings or reviews of bank products?**

Conclusion

As social commerce sites evolve, risk management professionals will need to be especially nimble to keep up with the issues that arise in the realms of regulatory compliance, information security, technology, and general risk management areas such as reputation risk. Remaining in the information loop within the institution is the key to analyzing these risks and responding to them in a timely and appropriate manner. Compliance professionals play an essential role in establishing a risk management review process that encompasses all of the bank's social commerce activity. BC

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