Consumer Compliance Supervision Bulletin - December 2019

This Federal Reserve publication provides high-level summaries of consumer compliance issues for senior executives in banking organizations and serves to complement other aspects of the Federal Reserve's outreach program for its supervised institutions, including *Consumer Compliance Outlook*, a Federal Reserve System publication focused on consumer compliance issues, and its companion webinar series, *Outlook Live*.

The Federal Reserve Board's Division of Consumer and Community Affairs publishes the *Consumer Compliance Supervision Bulletin* to enhance transparency regarding the Federal Reserve's consumer compliance supervisory activities by

- sharing information about our examiners' observations and noteworthy developments related to consumer protection, and
- providing practical steps that institutions may consider when addressing certain consumer compliance risks.

This issue of the *Consumer Compliance Supervision Bulletin* discusses Federal Reserve supervisory observations regarding financial technology, otherwise known as "fintech," which is simply the use of technological innovation to provide financial products and services.

Fintech has the potential to provide significant benefits to consumers, small businesses, and financial institutions. Yet the use of technology related to consumer financial services is not immune to the same consumer protection risks that occur in more traditional financial services and may pose new risks. The good news is that most banks can use their existing experience in consumer compliance management to evaluate a new fintech collaboration or fintech activity. This resource is intended to enhance the understanding of common fact patterns and emerging risks so that institutions can manage fintech risk appropriately and efficiently.

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Managing the Fair Lending Risks of Targeted Internet-Based Marketing

Sophisticated technology- and data-driven techniques have made it easier for businesses—including financial institutions—to target marketing to particular segments of consumers. Fair lending risks may arise from internet-based targeted marketing. We are still learning about how these platforms handle advertising, and it is an area that warrants attention. We offer some strategies that may help banks manage risk as our understanding of these issues continues to develop.

Background and Observations

Businesses now have access to sophisticated advertising analytics to help them reach specific segments of their markets. The algorithms that determine which ads a particular consumer sees are often based on highly detailed consumer profiles culled from such sources as website browsing histories, retailers, and credit card providers. Advertisers use these consumer data to target consumers by their locations, online habits, or the activities that they are predicted to engage in in the future.[17] Using these analytics has resulted in websites displaying higher prices to some consumers based on perceptions about consumer preference due to, for example, the type of computer operating system used and websites varying a product's price or availability based on geography.[18]

While targeted advertisements may offer benefits to consumers, targeted marketing based on consumer data can raise a range of consumer protection and fair lending risks. When the advertisements displayed via the internet vary by individual, we can no longer assume that consumers will broadly have access to the same options, even if they were to do their best to research and seek out as many choices as possible online. Unequal access to information about credit can raise fair lending risks and lead to redlining or steering as discussed below.

Fair Lending Risk and Internet-Based Targeted Marketing

The Federal Reserve enforces the two primary federal laws that ensure fairness in lending: the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA).[19] Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Federal Reserve has supervisory authority under the ECOA for state member banks with assets of $10 billion or less. For all state member banks, regardless of asset size, the Federal Reserve enforces the FHA.

The ECOA prohibits credit discrimination on the basis of race, color, religion, national origin, sex, marital status, age, receipt of income from any public assistance program, or because a person has exercised certain legal rights under the ECOA and other financial statutes. The ECOA and its implementing regulation apply to both consumer and commercial credit. Through Regulation B, the ECOA prohibits creditors from making oral or written representations in advertising or other formats that would discourage, on a prohibited basis, a reasonable person from making or pursuing a credit application.[20]

The FHA applies to credit related to housing and prohibits discrimination on the basis of race or color, national origin, religion, sex, familial status, and handicap. With respect to marketing, the FHA prohibits discrimination in advertising regarding the sale or rental of a dwelling, which includes credit discrimination.[21]

Both laws prohibit redlining, which is a form of illegal discrimination in which an institution provides unequal access to credit based on the race, color, or national origin of a neighborhood.[22] Fair lending laws also protect against the steering of an applicant to specific loan products based on prohibited characteristics, such as race or national origin, rather than the applicant's need or other legitimate factors.[23]

Recent developments regarding the social media company Facebook highlight the risks of relying on technology for advertising, including any advertising platform that uses algorithms or filters, without also considering the fair lending implications of such technology.

Facebook's Marketing Settlement with Civil Rights Advocates and Housing Discrimination Charge by HUD

A number of technology companies, including Facebook, provide sophisticated targeted marketing services to businesses seeking to advertise online. Facebook's advertising platform is designed to help businesses reach a "core target audience" based on consumers' locations, demographics, behavior, interests, and similarity to current customers.[24]

Investigations by a news organization concluded that Facebook's platform could result in ads that excluded viewers by characteristics such as race or gender. For example, it was possible to post a real estate ad that would not be shown to African American, Hispanic, or Asian American viewers or to post ads for a job driving for a car service that were only shown to male viewers.[25]

In March 2019, several civil rights and other organizations announced a settlement with Facebook over similar allegations that Facebook's advertising platform allowed discrimination in housing, employment, and credit advertising. The platform also allegedly allowed advertisers to limit advertising to narrow geographic areas and to target audiences of Facebook users with common characteristics with the advertiser's current customers or other groups (called a "Lookalike

Audience"), which the organizations argued could have a negative impact on various groups, including based on gender, race, and age.[26]

Also in March 2019, the U.S. Department of Housing and Urban Development (HUD) charged Facebook with housing discrimination as a result of the targeting and filtering practices permitted by the company's ad platform.[27] HUD also alleged that Facebook itself discriminates by using machine learning and other techniques to decide how and to whom to deliver specific advertisements. These practices included identifying which users would or would not see particular advertisements, varying the price of advertisements charged to advertisers based on the characteristics of the users who would see them, and classifying users in a way that is related to protected characteristics, such as sex or race.

Managing Risks

Both the Facebook settlement and HUD's discrimination charge underscore that fair lending laws apply equally to internet-based advertising as they apply to traditional advertising. Many of the considerations for developing traditional advertising also are present when developing online advertising.

While we are still learning about this issue, below are some steps that banks can take to manage this fair lending risk:

- reviewing for and eliminating any geographic filters used in internet-based advertising, such as filters by ZIP code or branch radius, that would exclude predominantly minority neighborhoods;
- reviewing other elective filters in use to ensure that the they do not prevent (even unintentionally) viewers with characteristics protected by the ECOA or the FHA from seeing an online ad;
- reviewing any information available from the internet-based advertising service regarding the audience that viewed each online ad;[28]
- establishing policies and procedures to evaluate fair lending risk for *all* marketing and outreach initiatives, including those that are internet-based and those that are not;
- monitoring marketing and outreach activities to ensure that those activities are reaching the entire assessment or credit market area, including any predominantly minority neighborhoods;
- ensuring that vendor management policies are in place; and
- understanding what marketing practices are being employed by the bank or on its behalf, and having appropriate controls to assess and manage any risk associated with those practices.[29]