



Banks, Savings & Loans, Credit Unions

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Background

Banks are only one of several kinds of financial institutions that offer financial services to their patrons. The term "bank" is often used as a collective term to describe any one of the numerous forms of financial institutions. Banks, like most other bank-like financial institutions, are established by charters. A charter is official permission from a regulating authority (like a state) to accept deposits and/or to provide financial services. Charters provide the specifics of a bank's powers and obligations. State and federal governments closely regulate banks and bank accounts. Accounts for customers may be established by national and state financial institutions, all of which are regulated by the law under which they are established.

The federal government regulated and controlled interest rates on bank accounts for many decades. There was a cap on interest rates for savings accounts, and most interest bearing payments—on—demand deposit accounts (e.g. checking accounts) were prohibited. Banks were also prevented from offering money market accounts. But sweeping changes in banking law in the early 1980s transformed the way banks and other financial institutions do business. For example, interest rate controls on savings accounts were eliminated by the **DEPOSITORY** Institutions Deregulation Act of 1980 (DIDRA), and the Garn-St Germain Depository Institutions Act and the DIDRA lifted restrictions on checking and money market accounts.

One common and important service offered by banking institutions is the checking accounts. Federal and state laws govern the operation of checking accounts. Article 4 of the **UNIFORM COMMERCIAL CODE**, which has been adopted at least in part by every state, enumerates the rights and obligations between financial institutions and their customers with respect to bank deposits and collections. The five principal sections of Article 4 cover the following:

1. General provisions and definitions
2. The actions of one bank in accepting the check of another and those of other banks that handle the check but are not responsible for its final payment
3. The actions of the bank responsible for payment of the check
4. The relationship between the bank responsible for payment of the check and its customers
5. The handling of documentary drafts, which are checks or other types of drafts that will only be honored if certain papers are first presented to the institution responsible for payment of the draft

Checks are commercial documents called "negotiable instruments." Negotiable instruments are mainly governed by Article 3 of the Uniform **COMMERCIAL CODE**. All states have adopted Article 3 of the Uniform Commercial Code (UCC), with some modifications, as the law governing negotiable instruments.

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Other types of negotiable instruments include drafts and notes. Drafts are documents ordering some type of payment to be made to a person or an institution. Checks are one kind of draft. Notes are documents promising payment will be made. A [MORTGAGE](#) is a kind of note. Money, investment [SECURITIES](#), and some forms of payment orders are not considered negotiable instruments under Article 3.

In the Great Depression, banks that could not meet their financial obligations to their customers or their creditors failed (became bankrupt). Because the deposits were not insured, individuals and businesses with money on deposit at the time a bank failed lost whatever was in the account at the time the bank failed. The depression and the banking crisis of the 1930's gave rise to the development of federal insurance for deposits administered by the Federal Deposit Insurance Corporation (FDIC). The program is funded from premiums paid by member institutions. Under the FDIC, individual bank accounts at insured institutions are protected up to \$100,000. Multiple accounts in a single financial institution and belonging to the same customer are combined for purposes of the FDIC limits.

Banks are strictly regulated by three federal agencies. Banks are also subject to regulation by state bank regulators.

The federal agencies are given below:

- COMPTROLLER of the Currency (for national banks)
- Federal Deposit Insurance Corporation
- Federal Reserve Board

States regulate banks through their banking commission or department of banking and finance. An official called the Commissioner or Director or Superintendent of Banks manages the state's banking commission or department of banking and finance. These state banking authorities may regulate only banks that have been chartered by the state.

The Gramm-Leach-Bliley Act, signed into law on November 12, 1999, is one of the most significant pieces of banking legislation in over fifty years. This law is the result of decades of effort to restructure the U. S. financial system. The Gramm-Leach-Bliley Act is complex and far-reaching, and contains a host of banking and financial services issues. Perhaps the most important feature of the Act is that it permits formal affiliations among banks, securities firms, and insurance companies. With the passage and implementation of these laws, the entire U. S. banking industry has been transformed. The U. S. banking system is innovative, yet it remains one of the safest, most secure systems in the world. It is also one of the most complex.

Types of Financial Institutions

Banks

In common parlance the term "bank" refers to many types of financial institutions. In addition to a bank, the term can refer to a [TRUST COMPANY](#), a savings bank, savings and loan institution, [CREDIT UNION](#), thrift, thrift and loan, or trust company

There is a wide variety of banking institutions. The differences among these financial institutions is the result of both history and politics. Some banks may be regulated and supervised by different federal and/or state agencies. While these institutions may appear quite similar, they actually have different rights, powers, and obligations; they may even have different tax obligations. Savings and loan associations must invest more of their assets in home mortgages than traditional banks. Trust companies manage and administer trust funds of

individuals and [PENSION](#) plans but may not take deposits into checking or savings accounts. Credit unions enjoy certain tax advantages. Some banking institutions have special deposit insurance arrangements. Some financial institutions can sell other financial services or products—like insurance—and other financial institutions may not. And some financial institutions must put significant cash reserves on deposit with the federal government, whereas others do not.

Banks that are chartered by the Comptroller of the Currency are called "National banks." National banks usually bear the words "national" or "national association" in their titles; sometimes they carry the letters N. A. or N. S. & T. in their titles.

Savings and Loan Institutions

The primary function of savings and loan associations is the financing of long-term residential mortgages. Savings and loan associations accept deposits in savings accounts, pay interest on these accounts, and make loans to residential home buyers. They do not make business loans of any kind, nor do they provide many of the other business services one finds in commercial banks. A privately managed home financing institution, a savings and loan accepts savings accounts from individuals and other sources. This money is then principally invested in loans for the construction, purchase, or improvement of homes.

Savings and loan associations are primarily involved in making residential loans. Consequently, they may be good sources of indirect business financing for homeowners who own substantial equity in their homes. For example, if homeowners need money for their businesses, they can refinance their homes or take out a second mortgage on the equity through a [SAVINGS AND LOAN ASSOCIATION](#). The home equity loan application process at a savings and loan association is generally simpler than it is for a commercial bank because it is made on the equity of the home up to a maximum percentage of the equity, usually between 75 percent to 80 percent. The savings and loan association bears little risk if the home is located in a stable or appreciating [MARKET VALUE](#) area. If the borrower defaults on the loan, the savings and loan association can foreclose the mortgage and, sell the property to retire the loan, doing so often for a profit.

Credit Unions

The first credit union in the United States was formed in Manchester, New Hampshire, in 1909. As of 2002, there are over 10,000 credit unions in the United States. They control assets of nearly one-half a trillion dollars and serve about one-quarter of the population. Credit unions are members-only institutions. Individuals must join a credit union to take advantage of its services. But they cannot join just any credit union—they must first be eligible for membership. Most credit unions are organized to serve members of a particular community, group or groups of employees, or members of an organization or association. Large [CORPORATIONS](#), unions, or educational institutions are some of the groups who commonly form credit unions for their members or employees.

Federal credit unions are nonprofit, cooperative financial institutions owned and operated by their members. Credit unions are democratically controlled with members given the opportunity to vote on important issues that affect the running of the credit union. For example, the board that runs a credit union is elected by its members. Credit unions provide an alternative to banks and savings and loan associations as safe places in which to place savings and borrow at reasonable rates. Credit unions pool their members' funds to make loans to one another.

In addition to typical credit unions that serve members and provide banking and lending services, there are a few special types of credit unions:

- Community development credit unions: The NCUA established the Office of Community Development Credit Unions in early 1994. These credit unions serve mostly low-income members in economically distressed and/or financially deprived areas. Part of their function is to educate their members in fundamental money management concepts. At the same time, they provide an economic base in order to stimulate economic development and renewal to their communities.
- CORPORATE credit unions: These institutions do not provide services to individuals, but they serve as a sort of credit union for credit unions. Nationwide, there are over thirty federally insured corporate credit unions; they provide investment, liquidity, and payment services for their member credit unions.

Automated Teller Machines (ATMs)

Not all banks or financial institutions have ATMs. Before ATMs, banks employed tellers to help their customers conduct all their banking business. Because ATMs can inexpensively perform many of the functions formerly done by tellers, ATMs have replaced many tellers in the banking institution. There are no laws requiring banks or other financial institutions to have ATMs. Instead, having one is a business decision for each bank. ATMs offer distinct advantages over traditional teller operations in terms of their locations and hours of operation. ATMs are relatively small and can be placed where banks would not ordinarily open a branch (gas stations, hotel lobbies, airports). Furthermore, ATMs are open when banks are closed; ATMs can function for twenty-four hours a day, seven days a week.

There has been a process of homogenization in the banking and financial industries. Services appear to be similar in many types of institutions. Nevertheless, some important differences among institutions remain. These differences may exist among banking institutions within a single state, and among the same type of institution from state to state. For example, a Missouri state chartered bank may have authority to conduct certain forms of business that are very different from those of a Missouri savings bank. Likewise, a Missouri savings and loan may have different powers from a Missouri national bank. These various rules and powers result in a difference in services among the spectrum of financial institutions. These differences can affect factors like interest rates, issuance of credit cards, ATM services, and so forth.

ATMs can be cost effective to operate when compared to the cost of hiring and training bank tellers. Even so, there are costs associated with owning and operating ATMs, including the costs for the following:

- Buying the machine
- Renting space for the ATM
- Maintaining the ATM's mechanical parts
- Paying personnel to load it with money and remove deposits (if any)

Banks or other financial institutions may charge patrons for using their bank's ATM as long as the bank or financial institution informs patrons of the terms and conditions of their accounts, and all applicable charges. This information is often contained in the monthly statements. On the other hand, if individuals use an ATM that does not belong to their own bank, the ATM's owner can charge them for using it. This is true even though they are gaining access to their own money kept in their own bank. Likewise, a bank can also charge its patrons for using someone else's ATM machine. In this way, individuals may incur two charges for using an ATM that does not belong to the bank or financial institution at which they are customers.

Federal Laws

There are many laws that apply to financial institutions. Most of these are found in Title 12 of the United States Code. Some of the most important laws are:

- 12 [USC](#) §§ 1461-1470: Laws regulating Federal Savings and Loan Associations
- 12 USC §§ 4001-4010: The Expedited Funds Availability Act
- 12 USC § 371a: Garn-St. Germain Depository Institutions Act
- 12 USC §§ 1811-1832: Federal Deposit Insurance Corporation
- 12 USC: Banks and Banking
- 28 USC § 1348: Banking Associations as Parties to Civil Litigation

In addition to statutes, there are administrative rules that govern financial institutions. These rules have the same force and effect as actual laws passed by Congress. Title 12 of the CODE OF FEDERAL REGULATIONS is the site of most federal agency regulations that deal with banks and banking.

Additional Resources

"*Bank and Thrift Rating Services for Consumers.*" <http://www.fdic.gov/bank/individual/bank/index.html>. FDIC, 2002.

Banking Law. Graham, Ann, ed., Matthew Bender, Inc., 1981.

"*Consumer Rights: Federal Laws.*" <http://www.fdic.gov/consumers/consumer/rights/index.html>. FDIC, 2002.

"*Federal Financial Institutions Examination Council.*" <http://www.ffiec.gov/>.

Organizations

American Bankers Association (ABA)

1120 Connecticut Avenue, N.W.
Washington, DC 20036 USA Phone: (800) 226-5377
E-Mail: custserv@aba.com
URL: <http://www.aba.com/default.htm>

Conference on State Bank Supervisors (CSBS)

1015 18th Street NW, Suite 1100
Washington, DC 20036 USA
Phone: (202) 296-2840
Fax: (202) 296-1928
URL: <http://www.csbs.org/>

Federal Depository Insurance Corporation (FDIC)

550 Seventeenth Street, NW
Washington, DC 20429 USA
URL: <http://www.fdic.gov/>

National Credit Union Administration (NCUA)

1775 Duke Street
Alexandria, VA 22314 USA
Phone: (703) 518-6300
URL: <http://www.ncua.gov/>

Office of the Comptroller of the Currency (OCC)

1301 McKinney Street, Suite 3710
Houston, TX 77010 USA
URL: <http://www.occ.treas.gov/>

Office of Thrift Supervision (OTS)

1700 G Street, NW
Washington, DC 20552 USA
Phone: (800) 842-6929
E-Mail: consumer.complaint@ots.treas.gov
URL: www.ots.treas.gov

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