ABCs of Banking
University of North Carolina School of Law

Why do we have Banks?

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MARCH 26, 2025

Topics for today

Are banks really any different from other businesses?

What good are banks—can we live without them?

What are their strengths and weaknesses?

Why does the Government regulate and supervise banks?

What Federal Agencies Regulate and supervise the banking industry and what do they do?

Ordinary companies

In the US, businesses operate in many forms, including as a sole proprietorship (i.e., a person conducting business directly) and through various types of corporate forms.

- Corporate forms include a stock corporation, a limited liability company, a general partnership, a limited partnership, a non-profit entity, and other entities with special tax treatment.
- Corporate forms have various tax advantages, make it easy to attract and organize a large numbers of investors, and provide some insulation to investors from liability for debts and many legal problems of the business, among other advantages.
- Corporate forms are primarily creatures of State law, that is, the permission to form a company, and the rules governing corporate governance and liability are typically determined by the State law where the company is formed and/or registered to conduct business. The Federal Government does not typically charter companies and there is no body of Federal corporate law.
- In the US, any person may conduct business through a corporate form. To form a company, a person must register with a state government, choose a form of corporate entity (such as a corporation, partnership, or limited liability company), choose a unique name and pay a small registration fee.

Once formed, a company may engage in <u>any activity</u> and conduct any business with a general corporate license, *<u>unless</u> that activity is specifically prohibited by law*.

A look at balance sheets of ordinary non-bank companies

Let’s look at some balance sheets of ordinary corporations, including some non-bank competitors of banks. In each case, notice:

Assets on the left side; liabilities and capital on the right side. The two sides must balance—that is, be equal.

Typically, the assets of a company include marketable securities and cash, accounts receivable and other things needed to run a business day-to-day, also goodwill—the premium paid for acquisitions. Cash is usually held as a deposit in a bank

The dominant liabilities are typically various forms of debt used to fund the business, such as accounts payable to others for goods purchased, various leases for property used in the business and debt incurred to fund business operations.

Notice in particular the amount of shareholders equity compared to the amount of total liabilities. Ordinary businesses typically have a significant amount of shareholders equity compared to total liabilities, meaning that shareholders largely fund the business operations of the company.

Meta, Inc

As of 12/31/2022, $ amounts in millions

Assets		
Current assets:		
Cash and cash equivalents	$	14,681
Marketable securities		26,057
Accounts receivable, net		13,466
Prepaid expenses and other current assets		5,345
Total current assets		59,549
Non-marketable equity securities		6,201
Property and equipment, net		79,518
Operating lease right-of-use assets		12,673
Intangible assets, net		897
Goodwill		20,306
Other assets		6,583
Total assets	$	185,727

Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$	4,990
Partners payable		1,117
Operating lease liabilities, current		1,367
Accrued expenses and other current liabilities		19,552
Total current liabilities		27,026
Operating lease liabilities, non-current		15,301
Long-term debt		9,923
Other liabilities		7,764
Total liabilities		60,014
Commitments and contingencies		
Stockholders' equity:		
Common stock, $0.000006 par value; 5,000 million Class A shares authorized, 2,247 million and 2,328 million shares issued and outstanding, as of December 31, 2022 and 2021, respectively; 4,141 million Class B shares authorized, 367 million and 413 million shares issued and outstanding, as of December 31, 2022 and 2021, respectively		—
Additional paid-in capital		64,444
Accumulated other comprehensive loss		(3,530)
Retained earnings		64,799
Total stockholders' equity		125,713
Total liabilities and stockholders' equity	$	185,727

Rocket Companies (Mortgage, Loans, Other)

As of 12/31/2022, $ amounts in thousands

Assets		
Cash and cash equivalents	$	722,293
Restricted cash		66,806
Mortgage loans held for sale, at fair value		7,343,475
Interest rate lock commitments ("IRLCs"), at fair value		90,635
Mortgage servicing rights ("MSRs"), at fair value		6,946,940
Notes receivable and due from affiliates		10,796
Property and equipment, net		274,192
Deferred tax asset, net		537,963
Lease right of use assets		366,189
Forward commitments, at fair value		22,444
Loans subject to repurchase right from Ginnie Mae		1,642,392
Goodwill and intangible assets, net		1,258,928
Other assets		799,159
Total assets	$	20,082,212

Liabilities and equity		
Liabilities:		
Funding facilities	$	3,548,699
Other financing facilities and debt:		
Lines of credit		—
Senior Notes, net		4,027,970
Early buy out facility		672,882
Accounts payable		116,331
Lease liabilities		422,769
Forward commitments, at fair value		25,117
Investor reserves		110,147
Notes payable and due to affiliates		33,463
Tax receivable agreement liability		613,693
Loans subject to repurchase right from Ginnie Mae		1,642,392
Other liabilities		393,200
Total liabilities	$	11,606,663
Equity:		
Class A common stock, $0.00001 par value - 10,000,000,000 shares authorized, 123,491,606 and 126,437,703 shares issued and outstanding as of December 31, 2022 and December 31, 2021, respectively.	$	1
Class B common stock, $0.00001 par value - 6,000,000,000 shares authorized, none issued and outstanding as of December 31, 2022 and December 31, 2021.		—
Class C common stock, $0.00001 par value - 6,000,000,000 shares authorized, none issued and outstanding as of December 31, 2022 and December 31, 2021.		—
Class D common stock, $0.00001 par value - 6,000,000,000 shares authorized, 1,848,879,483 shares issued and outstanding as of December 31, 2022 and December 31, 2021.		19
Additional paid-in capital		276,221
Retained earnings		300,394
Accumulated other comprehensive income		69
Non-controlling interest		7,898,845
Total equity		8,475,549
Total liabilities and equity	$	20,082,212

Jeffries Financial Group (Securities Broker Dealer)

As of 12/31/2022, $ amounts in thousands

ASSETS		
Cash and cash equivalents	$	9,703,109
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations		957,302
Financial instruments owned, at fair value (includes securities pledged of $14,099,136 and $12,723,502 at November 30, 2022 and 2021, respectively)		18,666,296
Investments in and loans to related parties		1,426,817
Securities borrowed		5,831,148
Securities purchased under agreements to resell		4,546,691
Securities received as collateral, at fair value		100,362
Receivables:		
Brokers, dealers and clearing organizations		1,792,937
Customers		1,225,137
Fees, interest and other		568,921
Premises and equipment		906,864
Goodwill		1,736,114
Other assets (includes assets pledged of $1,032,353 and $990,389 at November 30, 2022 and 2021, respectively)		3,595,985
Total assets	$	51,057,683

LIABILITIES AND EQUITY		
Short-term borrowings	$	528,392
Financial instruments sold, not yet purchased, at fair value		11,056,477
Securities loaned		1,366,025
Securities sold under agreements to repurchase		7,452,342
Other secured financings (includes $1,712 and $102,788 at fair value at November 30, 2022 and 2021, respectively)		2,037,843
Obligation to return securities received as collateral, at fair value		100,362
Payables:		
Brokers, dealers and clearing organizations		2,628,727
Customers		3,578,854
Lease liabilities		533,708
Accrued expenses and other liabilities		2,573,927
Long-term debt (includes $1,583,828 and $1,843,598 at fair value at November 30, 2022 and 2021, respectively)		8,774,086
Total liabilities		**40,630,743**
MEZZANINE EQUITY		
Redeemable noncontrolling interests		6,461
Mandatorily redeemable convertible preferred shares		125,000
EQUITY		
Common shares, par value $1 per share, authorized 600,000,000 shares; 226,129,626 and 243,541,431 shares issued and outstanding, after deducting 90,334,082 and 72,922,277 shares held in treasury		226,130
Additional paid-in capital		1,967,781
Accumulated other comprehensive loss		(379,419)
Retained earnings		8,418,354
Total Jefferies Financial Group Inc. common shareholders' equity		**10,232,846**
Noncontrolling interests		62,633
Total equity		**10,295,479**
Total liabilities and equity	$	**51,057,683**

Why do ordinary companies fail?

Usually, an ordinary company will fail due to a problem related to operations, financing or sales.

- Customers no longer are willing to buy products sold by the company, so revenues decline and the company can’t pay its business expenses and debts in an ongoing manner
- The company loses the ability to make its product (e.g., catastrophe or loss of supplier) or sell it at a reasonable price
- The company can no longer obtain credit needed to operate
- Failure is not usually a balance sheet problem
- Failure of an ordinary company is not usually a threat to financial stability or the economy

How is a depository institution different from an ordinary company?

<u>Depository Institutions are unique corporate entities</u>.

- A Depository Institution (DI) may be chartered by <u>*either*</u> a state <u>*or*</u> the Federal government, the chartering (and acquisition) process is rigorous and requires substantial capital at the start.
- A DI may engage in "the business of banking," and is granted <u>*three special powers*</u> not available to ordinary companies: the power to collect deposits protected by the US taxpayer, the power to access the US (and global) payments system; and the ability to access credit from the Federal Reserve discount window at any time (providing a source of funds whenever needed).
- <u>*Only*</u> an entity chartered by the state or Federal government <u>*as*</u> a DI may engage in a banking business (ordinary corporations may not collect deposits insured by the Federal government, do not have direct access to the payments system, and cannot borrow from the Federal Reserve except in extraordinary situations and then only on a limited basis).
- A DI may engage <u>*only*</u> in activities <u>*permitted*</u> by the chartering authority—not in general business activities.
- Because make deposits safe and retain confidence in the banking system, the US taxpayer (through the FDIC) guarantees deposit liabilities used by the DI in its activities.

What is special about depository institutions?

The Activities of a DI are especially important to the economy. DIs engage in activities as principal that are vital to the financial health of customers and the well being of the overall economy.

- Deposit-taking—this provides businesses, retail customers and others a safe place to temporarily store idle funds. Deposits are a type of debt liability of the DI—the DI has borrowed money from the depositor and owes the depositor the entire sum (deposits are NOT investments).
- Lending--this generates economic growth.
- Processing payments—processing checks, credit card transactions, and various types of wire transfers facilitates the safe and reliable transfer of funds throughout the economy.
- Intermediation and Maturity transformation--a DI helps make idle funds work for the economy and transforms short term liabilities into long term assets. In this way, a DI facilitates the efficient allocation and use of funds in the economy.

Concerns raised by DI activities.

- Abuse of economic power (e.g., biased or anti-competitive access to credit)
- Potential damage to the economy and to healthy DIs from the failure of a troubled DI.
- Because a DI is allowed to use customer deposits as well as investor equity to fund the DI's business activities, depositors may lose their funds if the DI fails.

The Balance Sheet of a depository institution reflects its uniqueness

The format of a bank's balance sheet is the same as for an ordinary company.

- Like any company, Assets are on the left side of the balance sheet,
- Liabilities and Shareholders Equity are on the right side of the balance sheet, and the two sides must be in balance.

Deposits are on both sides of the balance sheet.

- Deposits on the LEFT or Asset side reflect money the bank has deposited in another bank (just like for an ordinary company).
- Deposits are also by far the largest entry on the RIGHT or Liability side of the balance sheet. Banks fund their operations by taking deposits from customers and those deposits are legally debts owed to its customers.

The dominant asset on the balance sheet is loans extended to customers, then cash and investments in cash-like assets. For a bank, loans are the inventory of products from its operations.

Unlike with an ordinary company that makes profits mainly by selling its inventory, banks generate profits mainly by making and holding loans for the life of the loan.

- Banks may sell loans, but the amount of loans a bank will hold is typically driven by the amount of deposits it collects (that is, the amount of assets it holds is driven by the amount of deposits (Liabilities) it collects). An ordinary company manages its balance sheet differently—the amount of debt (Liabilities) it incurs is typically driven by the amount of assets it must hold and by the amount of cash it needs for its operations.

Compare the amount of Total Liabilities to Total Shareholders Equity. The ratio of Total Liabilities to Total Shareholders Equity is much smaller than for a typical ordinary company.

JPMC

As of 12/31/2022, $ in millions

Assets	
Cash and due from banks	$ 27,697
Deposits with banks	539,537
Federal funds sold and securities purchased under resale agreements (included **$311,883** and $252,720 at fair value)	315,592
Securities borrowed (included **$70,041** and $81,463 at fair value)	185,369
Trading assets (included assets pledged of **$93,687** and $102,710)	453,799
Available-for-sale securities (amortized cost of **$216,188** and $308,254; included assets pledged of **$9,158** and $18,268)	205,857
Held-to-maturity securities	425,305
Investment securities, net of allowance for credit losses	631,162
Loans (included **$42,079** and $58,820 at fair value)	1,135,647
Allowance for loan losses	(19,726)
Loans, net of allowance for loan losses	1,115,921
Accrued interest and accounts receivable	125,189
Premises and equipment	27,734
Goodwill, MSRs and other intangible assets	60,859
Other assets (included **$14,921** and $14,753 at fair value and assets pledged of **$7,998** and $5,298)	182,884
Total assets[a]	$ 3,665,743

Liabilities	
Deposits (included **$28,620** and $11,333 at fair value)	$ 2,340,179
Federal funds purchased and securities loaned or sold under repurchase agreements (included **$151,999** and $126,435 at fair value)	202,613
Short-term borrowings (included **$15,792** and $20,015 at fair value)	44,027
Trading liabilities	177,976
Accounts payable and other liabilities (included **$7,038** and $5,651 at fair value)	300,141
Beneficial interests issued by consolidated VIEs (included **$5** and $12 at fair value)	12,610
Long-term debt (included **$72,281** and $74,934 at fair value)	295,865
Total liabilities[a]	3,373,411
Commitments and contingencies (refer to Notes 28, 29 and 30)	
Stockholders' equity	
Preferred stock ($1 par value; authorized 200,000,000 shares: issued **2,740,375** and 3,483,750 shares)	27,404
Common stock ($1 par value; authorized 9,000,000,000 shares; issued **4,104,933,895** shares)	4,105
Additional paid-in capital	89,044
Retained earnings	296,456
Accumulated other comprehensive losses	(17,341)
Treasury stock, at cost (**1,170,676,094** and 1,160,784,750 shares)	(107,336)
Total stockholders' equity	292,332
Total liabilities and stockholders' equity	$ 3,665,743

What makes DIs fragile? Why do they fail?

The activities and funding of depository institutions are inherently risky.

- Maturity transformation activities greatly enhance economic activity, but they also introduce risky asset-liability mismatches.
- Access to cheap funding through deposit-taking activities is a strength and a source of fragility
- Management, operations and investor issues exist for DIs in the same way as for ordinary companies

Causes of failure of depository institutions

- **Capital insolvency**
  - Losses from lending activities
  - Losses from investment activities
  - Losses from operations (including from technical failures and from improper insider activities)
- **Liquidity insolvency**
  - Depositor runs resulting from loss of confidence in the institution
- **Operational failures**, very rare—typically cause either capital insolvency or liquidity insolvency.

Comparison of Key Financial Measures

	Total Assets	Net Income	Shareholder Equity	Leverage Ratio (Capital/Assets)	Net Income/ Total Assets
Meta, Inc	$185.727	$23.200	$125.713	67.69%	12.5%
Rocket Co.	$20.082	$0.699	$8.476	42.22%	3.5%
Jeffries Financial	$51.057	$0.782	$10.295	20.16%	1.5%
JPMC	$3,665.743	$37.676	$292.332	7.97%	1.0%
Wachovia Corp	$782.896	$6.312	$76.872	9.82%	0.8%
SVB Financial	$211.793	$1.609	$16.295	7.69%	0.76%

All Dollar figures in billions, and as of 12/31/2022 except Jeffries as of 11/30/2022 and Wachovia as of 12/31/2007

A Look at a Bank Failure: Capital Insolvency at Wachovia Bank

In 2007, Wachovia Bancorp was the fourth largest banking firm in the US with nearly $800 billion in total assets. It failed in early October, 2008, and is the largest bank failure in US history.

As shown on its 2007 year-end balance sheet, Wachovia Bank held over $457 billion in loans, mostly mortgages including a significant amount of subprime mortgage loans. (a net loans-to-total assets ratio of about 58.4%)

As the US housing market began its decline, Wachovia was forced to recognize almost $33 billion in losses during the first 6 months of 2008. To match the losses it recognized on its loan portfolio, Wachovia had to reduce its Shareholders Equity account by an equal amount—balance sheets must stay balanced and Wachovia remained legally obligated to repay depositors and other creditors.

That meant the Shareholders Equity account was cut nearly in half, from about $76.9 billion to about $44 billion. Both Wachovia management and the market expected Wachovia to take substantially more losses during the third quarter of 2008 as the housing market declined even more. With only $44 billion in remaining capital, Wachovia Bank was facing capital insolvency, that is, a total depletion of its capital. Wachovia was purchased by Wells Fargo in a deal brokered by the FDIC.

While Wachovia Bank had sufficient cash and cash equivalents to be able to pay its liabilities for some period of time, capital insolvency—a balance sheet calculation—is a grounds for closing a bank in order to stave off a run on the bank and further losses as the bank tries to raise funds by selling assets at depressed prices in a fire sale to meet a run.

An important lesson—Shareholders Equity is important because it is the cushion a bank has to absorb losses.

Wachovia Corp (BHC)

As of 12/31/2007, $ amounts in millions

ASSETS	
Cash and due from banks	$ 15,124
Interest-bearing bank balances	3,057
Federal funds sold and securities purchased under resale agreements	15,449
Total cash and cash equivalents	33,630
Trading account assets	55,882
Securities (amortized cost $116,327 in 2007; $109,589 in 2006)	115,037
Loans, net of unearned income ($7,900 in 2007; $7,394 in 2006)	461,954
Allowance for loan losses	(4,507)
Loans, net	457,447
Loans held for sale	16,772
Premises and equipment	6,605
Due from customers on acceptances	1,418
Goodwill	43,122
Other intangible assets	2,119
Other assets	50,864
Total assets	$782,896

LIABILITIES AND STOCKHOLDERS' EQUITY	
Deposits	
Noninterest-bearing deposits	60,893
Interest-bearing deposits	388,236
Total deposits	449,129
Short-term borrowings	50,393
Bank acceptances outstanding	1,424
Trading account liabilities	21,585
Other liabilities	19,151
Long-term debt	161,007
Total liabilities	702,689
Minority interest in net assets of consolidated subsidiaries	3,335
STOCKHOLDERS' EQUITY	
Preferred stock, Class A, 40 million shares, no par value; 10 million shares, no par value; none issued	—
Dividend Equalization Preferred shares, no par value, outstanding 97 million shares in 2007 and in 2006	—
Non-Cumulative Perpetual Class A Preferred Stock, Series I, $ 100,000 liquidation preference per share, 25,010 shares authorized	—
Non-Cumulative Perpetual Class A Preferred Stock, Series J, $1,000 liquidation preference per share, 92 million depositary shares issued and outstanding in 2007	2,300
Common stock, $3.33-1/3 par value; authorized 3 billion shares, outstanding 1.960 billion shares in 2007; 1.890 billion shares in 2006	6,534
Paid-in capital	56,149
Retained earnings	13,456
Accumulated other comprehensive income, net	(1,567)
Total stockholders' equity	76,872
Total liabilities and stockholders' equity	$782,896

A Look at a Bank Failure: Liquidity Insolvency at Silicon Valley Bank

Unlike Wachovia, Silicon Valley Bank (SVB) faced pressures on its liability side.

SVB focused on serving venture capital funds and start-up businesses. Between 2019 and 2021, SVB nearly tripled in size from about $70 billion to about $212 billion in total assets. SVB was NOT a significant lender—its net loan portfolio was valued at almost $74 billion out of more than $211 billion in total assets (a net loans-to-total assets ratio of about 35%)

During the end of 2022, SVB experienced some deposit outflows by its venture capital and tech start-up customers as rising interest rates put pressure on these customers to fund their operations internally. SVB was able to fund these early outflows using cash on hand and by liquidating about $21 billion of its holdings of US government securities and other liquid assets.

In early 2023, SVB announced that it would take a $1.8 billion loss related to the sale of its investment securities sold to handle outflows from deposit withdrawals and planned to raise about $2.25 billion in additional capital.

A combination of factors, including the announced losses, the concentration of customers in the VC and tech community, the relatively small remaining portfolio of liquid assets available for sale on SVB's balance sheet, and concerns about a downgrade by the credit-rating agencies, fueled by social media, caused depositors at SVB to become concerned about the liquidity at SVB.

The day after SVB's announcement of its plan to buttress its balance sheet, depositors withdrew about $40 billion. SVB expected orders for an additional $100 billion in withdrawals the next day. SVB would not have been able to fund those expected withdrawals, and was closed in anticipation of liquidity insolvency.

An important lesson—banks need liquidity to address the potential that depositors may demand their funds at any time.

SVB Financial Group

As of 12/31/2022, $ amounts in millions

Assets		
Cash and cash equivalents	$	13,803
Available-for-sale securities, at fair value (cost of $28,602 and $27,370, respectively, including $530 and $61 pledged as collateral, respectively)		26,069
Held-to-maturity securities, at amortized cost and net of allowance for credit losses of $6 and $7 (fair value of $76,169 and $97,227, respectively)		91,321
Non-marketable and other equity securities		2,664
Total investment securities		120,054
Loans, amortized cost		74,250
Allowance for credit losses: loans		(636)
Net loans		73,614
Premises and equipment, net of accumulated depreciation and amortization		394
Goodwill		375
Other intangible assets, net		136
Lease right-of-use assets		335
Accrued interest receivable and other assets		3,082
Total assets	$	211,793

Liabilities and total equity		
Liabilities:		
Noninterest-bearing demand deposits	$	80,753
Interest-bearing deposits		92,356
Total deposits		173,109
Short-term borrowings		13,565
Lease liabilities		413
Other liabilities		3,041
Long-term debt		5,370
Total liabilities		195,498
Commitments and contingencies (Note 21 and Note 26)		
SVBFG stockholders' equity:		
Preferred stock, $0.001 par value, 20,000,000 shares authorized; 383,500 and 383,500 shares issued and outstanding, respectively		3,646
Common stock, $0.001 par value, 150,000,000 shares authorized; 59,171,883 and 58,748,469 shares issued and outstanding, respectively		—
Additional paid-in capital		5,318
Retained earnings		8,951
Accumulated other comprehensive income (loss)		(1,911)
Total SVBFG stockholders' equity		16,004
Noncontrolling interests		291
Total equity		16,295
Total liabilities and total equity	$	211,793

Why does the Federal Government supervise and regulate DIs?

Federal Deposit Insurance

- Federally-backed deposit insurance is designed to create a safe place for small businesses and consumers to place cash needed for daily living.

Federal Supervision and Regulation

- Federal supervision and regulation of banking firms is designed to reduce the number and impact of failures of banking firms and create a safer financial system.
- Federal supervision and regulation also protects the taxpayer, who ultimately stands behind the deposit insurance provided to IDIs.

Combination

- Together, Federal deposit insurance and Federal supervision and regulation also help to maintain confidence in the financial system by reducing fear that the failure of a troubled DI may cause the failure of other DIs and other financial firms that might be healthy.

Caveat:

- The combination of Federal supervision and regulation, Federal deposit insurance and the way the Federal Government has responded to past DI failures, has also created the perception that some banking firms are too important to let fail. This disadvantages smaller banking firms and creates a perception the Government may not be willing to fulfill—which creates its own hazard.

How warm is the Federal Government's embrace?

Prudential Rules. Supervisors attempt to reduce the risks of failure of DIs with:

- Capital requirements
- Liquidity requirements
- Limits on risky activities
- Limits on lending activities and credit exposure to customers, affiliates, insiders and others
- Limits on expansion and size
- Requirements that DIs be run by competent and experienced management
- Regular reporting and on-site examination of policies, financial condition, activities, risk management, etc.

Other Rules. Banking firms are also subject to other more special-purpose supervisory and regulatory requirements, such as:

- Rules designed to protect consumers from over-pricing, fraud, abusive or unfair or deceptive trade practices by the organization, and
- Laws designed to implement laws prohibiting socially undesirable activities, such as money-laundering, supporting illegal activities and funding terrorist activities.

The Development of US Banking Laws

The development of US banking laws has occurred in layers throughout the last 150 years, largely in response to various banking crises. The result is a complex system of regulators and legal requirements that often overlap and create tensions in the way depository institutions and their affiliates are supervised and regulated. For example,

- The National Banking Act of 1864 created the Office of the Comptroller of the Currency (OCC) and the national bank charter in order to help finance the Civil War, giving the OCC regulatory and supervisory authority over national banks.
- The Federal Reserve Act of 1913 created the Federal Reserve System in response to the Panic of 1907, and gave the Federal Reserve some regulatory authority over national banks and state member banks.
- The Federal Deposit Insurance Act created the FDIC and Federal deposit insurance in 1935 in response to the massive number of bank failures that led to the Great Depression, giving the FDIC regulatory and supervisory authority over state banks that were not members of the Federal Reserve System.
- The Bank Holding Company Act of 1956 authorized the Federal Reserve to regulate and supervise companies that control banks (and all their affiliates) in order to prevent BHCs from creating risks for their banks and being used to evade various limitations on the geographic scope and activities of banks.
- The Dodd-Frank Act of 2010 was enacted to address weaknesses in the bank regulatory structure revealed by the Great Financial Criss of 2007-09.

Key Supervisors and Regulators of Banking Firms

Federal Regulatory Agencies. These layers of laws have also created numerous Federal Agencies that interpret and enforce US Banking Laws. Some Agencies supervise or regulate specific activities, others supervise or regulate firms based on their charter type. The result is a complex system of agencies and laws that often overlap.

Key supervisors and regulators of depository institutions include:

- The Office of the Comptroller of the Currency (OCC).
- The Federal Reserve System, which is comprised of the Board of Governors (a Federal agency based in Washington DC) and 12 Federal Reserve Banks located across the US.
- The Federal Deposit Insurance Corporation.
- The National Credit Union Administration.
- State Banking Supervisors.
- The Consumer Financial Protection Bureau.

Coordination among Federal and State Agencies

- The Federal Reserve, FDIC and OCC generally coordinate their regulatory and supervisory activities in order to limit differences in supervision and regulation at the Federal level.
- The Federal Reserve and FDIC also coordinate with State bank supervisors on examinations of state-chartered banks and thrifts to reduce duplication and coordinate findings regarding the operations of state-chartered banks and thrifts.
- While the Agencies try to coordinate their regulatory and supervisory activities, conflicts and inconsistencies inevitably occur that add complications and uncertainty to banking regulation and supervision.

The Office of the Comptroller of the Currency (OCC)

Charters national banks

Supervises and examines national banks

- National banks are generally examined annually
  - National banks with less than $3 billion in total assets and good exam ratings are examined every 18-months, with more off-site review
  - Large National banks are examined continuously

Conducts Prudential supervision and regulation of national banks

- Sets capital, liquidity, stress testing and other prudential requirements
- Establishes and monitors compliance with risk management, corporate governance, internal controls, audit and compliance systems requirements

Activities regulation

- Determines the scope and type of activities permissible for national banks

Reviews expansion proposals

- Prevents monopoly or significant loss of competition; ensures strong resulting firms; encourages community lending

Foreign banks. Licenses, supervises and regulates federal US branches and offices of foreign banks

The Federal Deposit Insurance Corporation (FDIC)

Supervision and Regulation Authority.

- The Federal Deposit Insurance Corporation supervises State chartered banks that do not choose to become members of the Federal Reserve System. All state-chartered banks that collect insured deposits must choose either to be supervised and regulated by the Federal Reserve System or by the FDIC as a quid pro quo for taking deposits insured by the FDIC.
- Examinations, Prudential Supervision authority and Review of Expansion Proposals mirror OCC authority, but extend to State non-member banks only.
- The FDIC also examines all state-chartered savings associations and savings banks (thrifts).

Deposit Insurance.

- In addition to its role as a bank supervisor and regulator, the FDIC is empowered to insure deposits held by banks and thrifts, and has authority to resolve any failed bank and thrift that holds insured deposits.

Resolution Authority.

- The FDIC has authority to resolve all failed and failing insured depository institutions (banks and thrifts). It may not resolve a bank holding company or any non-bank affiliate of a bank except in extraordinary circumstances where FDIC action is necessary to prevent system risk.

The Federal Reserve System

Supervision and Regulation Authority.

- The Federal Reserve System supervises and regulates all state-chartered banks that choose to become part of the Federal Reserve System.
- The Federal Reserve also supervises and regulates all companies that acquire control of a bank (called a "bank holding company" or BHC) or thrift (called a savings and loan holding company or SLHC) Supervision and regulation of BHCs and all non-IDI subsidiaries of a BHC or SLHC.
- The Federal Reserve's Examinations, Prudential Supervision Authority and review of Expansion Proposals mirror OCC authority, but applies only to BHCs (and their non-banks subsidiaries) and State member banks.
- The Federal Reserve also supervises and regulates branches and agencies of foreign banks operating in the US.
- The Federal Reserve is responsible for adopting rules that govern transactions between a bank and its affiliates (Regulation W) as well as rules that govern transactions between a bank and insiders of the bank (Regulation O). These rules are then enforced by the primary Federal regulator of the bank.

Central Bank of the US

- The Federal Reserve is also charged with implementing monetary policy in order to maximize long term economic growth and maximum employment; maintaining a ubiquitous payment system for financial transactions; and serving as the lender-of-last resort for banks and, in emergency circumstances, to markets.

The Consumer Financial Protection Bureau

The CFPB

- Created by the Dodd-Frank Act to consolidate consumer regulation in one agency (enforcement still shared)

Brief overview of duties

- The CFPB interprets and enforces laws focused on financial services provided to consumers by any financial services provider (not just DIs):
  - Unfair and Deceptive Acts and Practices (UDAP),
  - Unfair, Deceptive, or Abusive Acts and Practices (UDAAP),
  - Ability to repay mortgage loans,
  - Truth in Lending Act (TILA) and Truth in Savings Act (TISA),
  - A variety of other consumer protection statutes.

Compliance examinations and enforcement

- By the CFPB for banking firms with more than $10 billion in assets and all non-banking firms
- By the Fed/OCC/FDIC for banking firms with $10 billion or less in total assets

Where to find the law: Statutes

National Bank Act	12 USC § 1
Federal Reserve Act	12 USC § 241
International Banking Act of 1978	12 USC § 1301
Home Owners Loan Act	12 USC § 1461
Federal Credit Union Act	12 USC § 1751
Federal Deposit Insurance Act	12 USC § 1811
Bank Holding Company Act	12 USC § 1841

Other laws, like the Gramm-Leach-Bliley Act and the Dodd-Frank Act, largely amend these and other statutes

Where to find the law: Regulations

Comptroller of the Currency Rules (National banks and thrifts)	12 CFR 1-199
Federal Reserve Rules (State member Banks, Bank Holding Companies, Savings and Loan Holding Companies, Foreign Banks, and Limits on transactions with affiliates and for insiders for all banks)	12 CFR 200s (Rules are referred to by Letter, with each letter matching the numerical designation—e.g., Regulation W is 12 CFR 223—the 23rd letter of the alphabet)
FDIC (State non-member banks, State thrifts, Deposit Insurance, Failed IDI resolutions)	12 CFR 300s
National Credit Union Administration (Federal regulation of credit unions)	12 CFR 700s
Consumer Financial Protection Bureau	12 CFR 1000s

Where to find the law: Agency websites

www.occ.treas.gov

www.federalreserve.gov

www.fdic.gov

www.ncua.gov

www.consumerfinance.gov