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Financial Institutions and Markets: Major Federal Statutes

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Abstract. This report provides summaries of the major federal laws affecting financial institutions and markets. Arrangement is chronological according to the order of original enactment, with divisions into three periods. The first period begins with the Civil War era and includes the creation of national banks and the Federal Reserve System. The second period encompasses the New Deal and its aftermath, during which a wall was erected and reinforced between commerce and banking. The third or current period is characterized by statutes designed to modernize the financial services industry and, consistent with safety and soundness, eliminate barriers to the provision of nationwide integrated financial services. In the interest of national security, criminal law enforcement, and protecting personal privacy, the current period is also marked by increased federal regulation of customer information maintained by financial institutions.

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Financial Institutions and Markets: Major Federal Statutes

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Research
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Financial Institutions and Markets: Major Federal Statutes

Summary

This report provides brief summaries of the major federal laws affecting financial institutions and markets. Arrangement is chronological according to the order of original enactment, with divisions into three periods. The first period begins with the Civil War era and includes the creation of national banks and the Federal Reserve System. The second period encompasses the New Deal and its aftermath, during which a wall was erected and reinforced between commerce and banking. The third or current period is characterized by statutes designed to modernize the financial services industry and, consistent with safety and soundness, eliminate barriers to the provision of nationwide integrated financial services. In the interest of national security, criminal law enforcement, and protecting personal privacy, the current period is also marked by increased federal regulation of customer information maintained by financial institutions.

For CRS reports on current topics, consult the "Financial Sector" subheading under "Current Legislative Issues" on the CRS home page: [http://www.crs.gov/].

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Background[2]

The history of federal legislation significantly affecting banking, securities, capital markets, and financial services in general, may conveniently be divided into three chronological periods: Civil War to New Deal; New Deal Era; and, 1956 to the present. Examination of these laws reveals that the increasing role of the federal government in overseeing and protecting financial services has been primarily in response to turmoil or financial distress in the economy. For example, landmark legislation brought a greater federal presence into the financial arena to moderate the financial stress and adversity of the Civil War, the financial Panic of 1907, the Great Depression of the 1930's, and the savings and loan crisis of the 1980's. Much of this legislation persists, albeit in amended form, and can be viewed as the foundation of the structure under which the financial services industry operates today.

Pre-New Deal legislation set up basic, continuing, entities, including the national banking system; the Federal Reserve System; and, in 1932, the Federal Home Loan Bank System. New Deal era legislation is probably most striking for its rigid separation of banking, securities, and insurance businesses, and for setting up major parts of the federal financial safety net, particularly deposit insurance. More recent legislation has permitted reintegration of these functions, allowing firms to compete across political boundaries, and in nontraditional businesses. The overall aim has been to produce a more level competitive "playing field" and continue to maintain safety. The effect has been generally to produce an increasingly more uniform structure of U.S. financial providers. Especially in the last two decades, laws have progressively "deregulated" New Deal or earlier controls over geography, pricing, and products of banking and financial services providers. The growing complexities of financial transactions have prompted financial services companies to maintain data bases containing large amounts of information on their individual customers, raising a potential for improper use. This has prompted increasing federal regulation of customer financial information to protect customer privacy, deter criminal activity, and in the interest of national security.

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[1] For CRS reports on current topics, consult the "Financial Sector" subheading under "Current Legislative Issues" on the CRS home page: [http://www.crs.gov].

[2] The author of this section is William D. Jackson, Specialist in Financial Institutions, Government and Finance Division.

The laws cited are those chosen for their historical significance, their present importance in the federal scheme of regulating financial services businesses, or their recent enactment.

Pre-New Deal Legislation

National Bank Act. 12 U.S.C. §§ 21-215b. This act establishes the national banking system and prescribes a comprehensive system of regulation for federally chartered banks, under the supervision of the Comptroller of the Currency within the U.S. Treasury Department. It was originally enacted during the Civil War by the National Bank Act of 1863 (Currency Act) (12 Stat. 665), and was significantly amended by the National Bank Act of 1864 (13 Stat. 99). Congress enacted the original measure to assist the Government in paying Civil War debts, to provide for chartering banks by the Federal Government, and to provide a more uniform national currency (as bank notes) and safer banks based on their holding U.S. Government bonds. The 1864 legislation included major amendments, among them requiring that national banks be incorporated and initiating a system of examining national banks. Under the National Bank Act, the federal government, through the Office of the Comptroller of the Currency (OCC), charters and regulates national banks, granting them powers and subjecting them to federal supervision.

Federal Reserve Act. 12 U.S.C. §§ 221-552. Originally enacted in 1913 and amended substantially since then, this legislation provides the authority for the Federal Reserve System — the Board of Governors of the Federal Reserve System (Federal Reserve Board), the 12 Federal Reserve Banks, and the Federal Open Market Committee. To prevent recurrence of another financial panic such as that of 1907, Congress designed "the Fed" to provide a better national payments system, including a national currency through its issuance of Federal Reserve notes. Another vital component of this payment system is the Federal Reserve's services to its member banks. These include clearing checks and other payments and lending to cash-short banks. The Board of Governors also exercises authority under various other federal laws, centralizing significant regulatory power over state banks that choose to join it as members, large financial conglomerates, and many international banking organizations operating on a nationwide basis.

Federal Home Loan Bank Act. 12 U.S.C. §§ 1421-1449. Originally enacted in 1932, this legislation established the Federal Home Loan Bank System to provide federal support for home mortgage lending. The Federal Home Loan Bank System parallels, for thrift institutions, such as the early savings and loan or building and loan associations, the Federal Reserve System for commercial banks. The Home Owners' Loan Act expanded it in 1933 to authorize federally-chartered thrift institutions. Originally, the Federal Home Loan Bank Board regulated the 12 Federal Home Loan Banks, and was the chartering authority for federal thrifts. In its capacity as head of the Federal Savings and Loan Insurance Corporation, the Bank Board provided a measure of federal regulation for state-chartered thrifts.

Today, after the enactment of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989, and the abolition of the Federal Home Loan

Bank Board, the system's 12 Federal Home Loan Banks are subject to the authority of the Federal Housing Finance Oversight Board. The Office of Thrift Supervision in the Department of the Treasury charters and regulates federally-chartered thrifts and provides federal supervision for state-chartered thrifts. See Home Owner's Loan Act, Financial Institutions Reform, Recovery, and Enforcement Act.

New Deal Legislation

Home Owners Loan Act of 1933. 12 U.S.C. §§ 1461-1470. This legislation was the authority for the creation and regulation of federal savings and loan associations. Originally chartered by the Federal Home Loan Bank Board as mutually owned and managed institutions owned by their depositors, federal savings and loan associations were largely restricted to residential mortgage lending. Today's federal savings associations are chartered and regulated by the Office of Thrift Supervision of the Department of the Treasury (OTS).

Banking Act of 1933. 48 Stat. 162. This early legislation of President Roosevelt's New Deal included many amendments to the Federal Reserve Act and the National Bank Act including the creation of the Federal Open Market Committee, which regulates and coordinates the purchase and sale of securities by Federal Reserve Banks. Four sections of the Banking Act of 1933, §§ 26, 20, 21, and 32, are known as the Glass-Steagall Act. Collectively, they forced a separation between the banking and securities businesses. Other parts of the legislation allowed national banks to open branches under limited conditions and began federal deposit insurance for banks under § 12B of the Federal Reserve Act before the enactment of the Federal Deposit Insurance Corporation Act in 1950.

Federal Deposit Insurance Act. 12 U.S.C. §§ 1811-1832. Enacted in the Banking Act of 1933 as part of the Federal Reserve Act, Congress made this legislation a separate law in 1950, 64 Stat. 873. The legislation authorizes the Federal Deposit Insurance Corporation (FDIC) to provide insurance for deposits held in state and national banks and branches of foreign banks in the United States. In enacting this legislation, the federal government took on the role of protecting depositors, banks, and the national money stock (and, thus, the economy) against losses from bank failures. Enactment of this legislation stopped the cascading string of bank failures of the Great Depression. Under this legislation, the FDIC is the primary federal regulator of federally-insured state-chartered banks and, as such, has authority to examine and set safety and soundness standards for them and, to some extent, for federally chartered institutions.

Securities Act of 1933. 15 U.S.C. §§ 77a-77aa. The Securities Act of 1933 has two objectives: (1) to provide investors with financial and other information concerning securities offered for public sale; and (2) to prohibit misrepresentation, deceit, and other fraudulent acts and practices in the sale of securities. The act provides for the registration of securities offered for sale in interstate commerce or through the mail and prohibits fraud in the sale of securities. It requires publicly traded companies to provide prospectus disclosures that permit investors and others to evaluate the worth of the stocks and bonds being sold. Its anti-fraud provisions apply to specified securities sold to the public even when the dealers that are offering them need not register them. Since 1934, the Securities Act of 1933 has been enforced by the Securities and Exchange Commission.

Securities Exchange Act of 1934. 15 U.S.C. §§ 78a-78kk. This legislation created the Securities and Exchange Commission (SEC) to enforce the federal securities laws. With the enactment of this legislation, businesses and their financial operations became subject to federal disclosure standards, thus, moving beyond state incorporation and investor protection standards. This act brought many securities markets under uniform federal regulation. It extended the registration and disclosure requirements of the Securities Act of 1933. Under the 1934 Act, every company with securities listed and registered for public sale on a national exchange and other companies meeting certain asset or number-of-shareholder criteria must file a registration application with the exchange and with the SEC. The legislation defines SEC's authority with respect to such matters as national exchanges, proxy solicitations, insider trading, margin trading, and registration of stock exchanges and broker-dealers in the over-the-counter market. It defines certain rules for corporate governance, including registration of securities listed on exchanges and publication of financial reports.

National Housing Act of 1934. 48 Stat.1246. This legislation created the Federal Housing Administration and established deposit insurance for savings and loan associations, through the Federal Savings and Loan Insurance Corporation (FSLIC). The Financial Institutions Reform, Recovery, and Enforcement Act abolished FSLIC in 1989 after widespread failures in the savings and loan industry. Currently, deposit insurance for savings and loan associations is provided through the Federal Deposit Insurance Corporation.

Federal Credit Union Act. 12 U.S.C. §§ 1751-1790. This legislation, originally enacted in 1934, provides a comprehensive system for the chartering and supervision of federal credit unions. Congress has transferred oversight of credit unions to various executive branch agencies over the years.

Currently, the National Credit Union Administration (NCUA) regulates credit unions. This agency oversees deposit insurance for both federal credit unions and state-chartered credit unions through an amendment in 1970. In 1979, P.L. 95-630 gave the NCUA oversight of a Central Liquidity Facility providing short-term federally sponsored funding to credit unions, as a lender of last resort conceptually similar to the Federal Reserve Banks and the Federal Home Loan Banks. Credit unions, which are cooperative in nature and, thus, not subject to corporate taxes, were initially very small and state-chartered. Federal support and various amendments to the Federal Credit Union Act have increased their powers and allowed them to become safer, more bank-like, and larger institutions serving their members. They remain limited in some of their services and customer bases.

Investment Company Act. 15 U.S.C. §§ 80a to 80a-52. Enacted in 1940, this legislation provides the Securities and Exchange Commission with authority to regulate investment companies, i.e., companies in the business of investing, reinvesting, or trading in securities, such as mutual funds or investment trusts, that offer their own securities to the public. This act initiated federal oversight over state-incorporated prototypes of mutual funds, whose weaknesses had become apparent in the Depression, by requiring that these companies register their securities, disclose policies and procedures, maintain adequate capital, and avoid insider transactions.

Investment Advisers Act of 1940. 15 U.S.C. §§ 80b to 80b-20. This legislation provides for the registration and regulation of investment advisors, i.e., persons who, for compensation, engage in the business of advising others, directly or through publications or writings, as to the value of securities or the advisability of investing in or selling securities. Its enactment completed the circle of federal regulation over most securities businesses especially when, in 1970, P.L. 91-547, extended the authority that the SEC exercised over broker-dealers to investment advisers.

McCarran-Ferguson Act. 59 Stat. 33, 15 U.S.C.§§ 1011-1015. Originally enacted in 1945, this legislation assigns the regulation of the business of insurance to the states, with an exception for Acts of Congress that specifically relate to insurance. In *United States v. South-Eastern Underwriters Association,* 322 U.S. 533 (1944), in determining whether a federal antitrust law was applicable to a group of insurance companies, the Supreme Court ruled that insurance was commerce and, thus, subject to regulation by Congress. McCarran-Ferguson was enacted in response to this decision, which had the potential to federalize the business of insurance. At the time, insurance was viewed more as a protective service business than as a "financial" service industry.

Post-New Deal Legislation

Bank Holding Company Act. 12 U.S.C. §§ 1841-1850. Originally enacted in 1956 to cover any company controlling more than one bank, and amended in 1970 to extend to one-bank holding companies, this legislation subjects companies controlling banks to a scheme of regulation administered by the Board of Governors of the Federal Reserve System. It prohibits such companies from engaging in certain non-banking activities. It provides centralized regulation over mixing of banking and commerce that was intended to increase the safety, soundness and competitive position of operations that had previously been the subject of state regulation alone. It became a template for financial modernization embodied in P.L. 106-102, the Gramm-Leach-Bliley Act.

Bank Secrecy Act of 1970/Currency and Foreign Transactions Reporting Act. Titles I and II of P.L. 91-508, including 12 U.S.C. §§ 1829b, and 1951 - 1959; 31 U.S.C. §§ 5311 et seq. The Bank Secrecy Act of 1970 and its major component, the Currency and Foreign Transactions Reporting Act, 31 U.S.C. §§ 5311 et seq., require reports and records of transactions involving cash, negotiable instruments, or foreign currency and authorize the Secretary of the Treasury to prescribe regulations to ensure that covered entities maintain adequate records of transactions that have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings. Violations of the regulations are subject to civil and criminal penalties. Congress thus extended federal oversight of financial arrangements to individual transactions when in the national interest.

Fair Credit Reporting Act. 15 U. S.C. §§ 1681-1681v. Originally enacted in 1970, this legislation regulates the credit reporting industry by prescribing standards that address information collected by businesses that provide information used to determine eligibility of consumers for credit, insurance, or employment. It imposes requirements for accuracy, limits purposes for which such information may be disseminated, prescribes certain access rights, and includes civil penalties for its violation. Overall enforcement authority resides with the Federal Trade Commission, but other federal agencies, including those that regulate financial institutions, are authorized to enforce the act with respect to persons under their jurisdiction. Consumer reporting agencies and users of information who willfully or negligently fail to comply with the act may be subject to civil liability.

Community Reinvestment Act of 1977. 12 U.S.C. §§ 2901-2907. This legislation requires federal banking regulators, in connection with an examination of a depository institution (bank, savings institution, or holding company for either), to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, and to consider that assessment when the institution applies for a deposit facility (branch, relocation of offices, change of corporate control such as merger and acquisition).

International Banking Act of 1978. 12 U.S.C. §§ 3101-3108. This measure, as amended by the Foreign Bank Supervision Enhancement Act of 1991, 105 Stat. 2286, provides for the chartering and regulation of foreign bank operations in the United States, permitting federal or state chartering of foreign bank branches and agencies, and regulation by the Board of Governors of the Federal Reserve System.

Financial Institutions Reform, Recovery, and Enforcement Act of 1989. 103 Stat. 183 (P.L. 101-73). This omnibus legislation, consisting of 12 titles, restructured the deposit insurance system; transformed the regulatory structure of savings associations by eliminating the Federal Home Loan Bank Board; reformed the Federal Home Loan Bank System, including eliminating the Federal Savings and Loan Insurance Corporation; prescribed rules for administering a depository institution in receivership or conservatorship; and expanded civil and criminal enforcement authority for depository institution offenses.

Federal Deposit Insurance Corporation Improvement Act of 1991. 105 Stat. 2236 (P.L. 102-242). This omnibus legislation provides expanded enforcement authority for federal banking regulators, including prompt corrective regulatory action to enforce capital standards on depository institutions to ensure institutional safety and soundness. It has meant greater uniformity of chartering, regulation, and supervision of both commercial banks and savings associations. It provides for greater federal supervision of state banks and state savings associations through the Federal Deposit Insurance Corporation.

Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. 108 Stat. 2338 (P.L. 103-328). This legislation provides the authority and sets the framework for bank holding companies to acquire banks outside their home states and for banks to acquire branches on an interstate basis. It overrode longstanding state prohibitions against nationwide banking, which had already been weakening via regional interstate banking compacts.

Gramm-Leach-Bliley Act. 113 Stat. 1388 (P.L. 106-102). This legislation authorizes financial holding companies and eliminates many state and federal barriers to affiliation among banks, securities firms, insurance companies, and other financial service providers. It provides for functional regulation by activity and thus specifies, for example, conditions under which securities activities of banking organizations are regulated by securities regulators. It sets the framework for insurance activities by banking organizations, prevents the creation of new "unitary" savings and loan holding companies mixing banking and commerce, modifies the membership criteria and capital structure of the Federal Home Loan Bank System, sets a framework for potentially establishing a National Association of Registered [Insurance] Agents and Brokers, requires certain disclosures about automatic teller machine (ATM) fees, establishes sunshine (disclosure) requirements for entities involving Community Reinvestment Act contracts with banking organizations, and includes various banking regulatory reforms. Its privacy title mandates that financial institutions disclose their privacy policies; requires them to protect the security and integrity of non-public personally identifiable information; and criminalizes obtaining customer information of financial institutions by fraud.

U.S.A. PATRIOT Act (Title III), International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001. P.L. 107-56. Congress has designed this legislation to prevent terrorists and others from using the U.S. financial system anonymously to move funds obtained from or destined for illegal activity. It authorizes and requires additional record keeping and reporting by financial institutions and closer scrutiny of accounts held for foreign banks and of private banking conducted for foreign persons. It requires financial institutions to establish anti-money laundering programs and imposes various standards on informal money transmitting businesses. It amends criminal anti-money laundering statutes and procedures for forfeitures in money laundering cases and requires further cooperation between financial institutions and government agencies in combating money laundering. It thus increases federal scrutiny of individual financial transactions and extends it to certain previously unexamined domestic and international transmitters of money, when in the national interest.

Sarbanes-Oxley Act of 2002. P. L. 107-204. Following the collapse of several major corporations, including Enron Corporation, Congress acted to protect investors and improve the reliability of corporate disclosures required under the securities laws. This legislation establishes the Public Company Oversight Board to regulate public accounting firms that audit publicly traded companies. It prohibits such firms from providing other services to such companies contemporaneously with the audit. It sets various corporate responsibility standards, including requirements that principal executive officers and principal financial officers (CEO's and CFO's) certify their publicly traded company's annual or quarterly report. The legislation authorizes, and in some instances requires, the Security and Exchange Commission (SEC) to issue rules governing improperly influencing audits, disgorgement of executive compensation related to misconduct involving accounting restatements, attorney reporting of material violations of securities laws, and securities analyst conflicts of interests. Pursuant to this law, insiders may no longer trade their company's securities during pension fund blackout periods; financial disclosure requirements are enhanced; and, there is increased authorization of appropriations for the SEC. It mandates various studies including a study of the involvement of investment banks and financial advisors in the scandals preceding the legislation and a report on enforcement actions. Also included are: whistle blower protections; new federal criminal laws, including a proscription against alteration of documents; various other enhancements of the tools to prosecute and punish securities fraud; and an extension of the statute of limitations for private securities fraud actions.

Check Clearing for the 21st Century Act. P. L. 108-100. This legislation, known as the Check 21 Act, is aimed at facilitating greater efficiency in the use of electronic processing of checks and check truncation. It permits the use of substitute checks by which a bank receiving a paper check may convert it to a form that may be processed electronically. The substitute check, rather than the original check, will be retained by the paying bank and returned to any bank customer receiving cancelled checks. The substitute check is defined to be a paper reproduction of an original paper check that contains an image of the front and back of the original check and that may be processed electronically. The legislation requires banks converting a paper check into a substitute check and other banks handling such checks to warrant the accuracy of the images and the fact that the check has not previously been paid. Such a substitute check is declared to be the legal equivalent of the original check for all purposes and all persons. The Check 21 Act includes indemnity and expedited recredit procedures to protect substitute check recipients. It does not require any bank to create substitute checks or to accept checks electronically.

Fair and Accurate Credit Transactions Act of 2003. P.L. 108-159. This legislation contains extensive amendments to the Fair Credit Reporting Act that are aimed at improving the accuracy and transparency of the national credit reporting system and preventing identity theft and assisting victims. It contains provisions enhancing consumer rights in situations involving alleged identity theft, credit scoring, and claims of inaccurate information. It requires users of consumer reports to provide certain information to consumers who are offered credit on terms that are materially less favorable than the offers that the creditor makes to a substantial portion of its consumers. Under the legislation, state laws respecting the sharing of consumer report information among affiliated companies are permanently preempted; such companies must provide consumers notice and an opt-out for sharing of such information if the receiving company uses the information for marketing purposes. Whether or not the information is used for marketing purposes, an opt-out must be provided consumers if the shared information contains anything other than experience or transaction information.

Federal Deposit Insurance Reform Act of 2005. P.L. 109-172, Title II, Subtitle B, §§ 2101-2108. This legislation merges the Bank Insurance Fund and the Savings Association Insurance Fund into the Deposit Insurance Fund (DIF). It increases deposit insurance coverage for certain retirement accounts to $250,000. It retains the $100,000 "standard maximum deposit insurance amount" of $100,000, but provides a process whereby deposit insurance coverage may be adjusted for inflation at five-year intervals beginning in 2010. There is also a provision that provides per-participant coverage to employee benefit plan accounts, even if the depository institution at which the deposits are placed is not authorized to accept employee benefit plan deposits. The legislation requires the FDIC to set the Designated Reserve Ratio within a range of 1.15% to 1.50% and declare dividends from the DIF when the DIF reserve ratio at the end of a calendar year equals or exceeds 1.35%. The legislation grants the FDIC Board the discretion to price deposit insurance according to risk for all insured institutions regardless of the level of the reserve ratio.