

Chapter 2

Government Policies and Regulation

Multiple Choice

1. Historically, a commercial bank was defined as a firm that:
- accepted NOW accounts and made consumer loans.
 - accepted demand deposits and made business loans.
 - accepted government deposits and made public loans.
 - accepted demand deposits and made consumer loans.
 - is regulated by the Federal Reserve.

Answer: b

2. Which of the following is not a purpose of bank regulation?
- Guarantee minimal profitability of the banking system.
 - Provide monetary stability.
 - Ensure safety and soundness of banks.
 - Provide a competitive financial system.
 - Protect consumers from abuses by banks.

Answer: a

3. A primary purpose of maintaining the safety and soundness of banks is to:
- encourage loan growth.
 - protect depositors.
 - ensure liquidity for the stock market.
 - prevent discrimination.
 - minimize bank losses.

Answer: b

4. Which of the following is not represented in the CAMELS ratings.
- Cash adequacy
 - Asset quality
 - Management quality
 - Liquidity
 - Sensitivity to market risk.

Answer: a

5. A formal regulatory document that prescribes corrective action for a problem institution is called a:
- a. cease and desist order.
 - b. capital request.
 - c. memorandum of understanding.
 - d. quality assurance directive.
 - e. national bank order.

Answer: c

6. A legal document that orders a firm to stop an unfair practice under full penalty of law is a:
- a. cease and desist order.
 - b. capital request.
 - c. memorandum of understanding.
 - d. quality assurance directive.
 - e. national bank order.

Answer: a

7. A new charter to start a state bank must be obtained from the:
- a. Federal Reserve.
 - b. Federal Deposit Insurance Corporation.
 - c. Office of the Comptroller of the Currency.
 - d. Office of Thrift Supervision.
 - e. State banking department.

Answer: e

8. A new charter to start a federal savings association is obtained from the:
- a. Office of the Comptroller of the Currency.
 - b. National Credit Union Administration.
 - c. Office of Thrift Supervision.
 - d. State banking department.
 - e. Federal Reserve

Answer: c

9. National and state charters are available for all of the following except:
- a. credit unions.
 - b. commercial banks.
 - c. savings associations.
 - d. Federal Reserve banks.
 - e. National and state charters are available for all of the above.

Answer: d

10. The primary federal regulator of state banks that are not members of the Fed is the:

- a. FDIC.
- b. Office of the Comptroller of the Currency.
- c. Office of Thrift Supervision.
- d. State's banking department.
- e. National Credit Union Administration.

Answer: a

11. The primary federal regulator of state banks that are members of the Fed is the:

- a. Resolution Trust Corporation
- b. Federal Reserve
- c. Office of the Comptroller of the Currency
- d. State Banking Authorities.
- e. Federal Deposit Insurance Corporation.

Answer: b

12. Commercial banks mostly specialize in:

- a. mortgages.
- b. mutual loans.
- c. short-term business credit.
- d. savings accounts.
- e. share draft accounts.

Answer: c

13. Savings and loans have historically specialized in:

- a. commercial loans.
- b. auto loans.
- c. mutual loan.
- d. real estate loans.
- e. demand deposit accounts.

Answer: d

14. Savings institutions must maintain what percent of their assets in housing-related assets to be considered a "Qualified Thrift Lender"?

- a. 100%
- b. 15%
- c. 70%
- d. 85%
- e. 65%

Answer: e

15. Many insurance companies have organized as a _____ in order to own a depository institution and bypass prohibitions in the Glass-Steagall Act and the Bank Holding Company Act.
- a. unitary thrift holding company
 - b. commercial bank
 - c. mortgage company
 - d. savings bank
 - e. credit union

Answer: a

16. Which of the following institutions' customers have a "common bond"?
- a. credit union
 - b. commercial bank
 - c. mortgage company
 - d. savings bank
 - e. thrift

Answer: a

17. Originally, the FDIC insured deposits up to:
- a. \$100,000
 - b. \$50,000
 - c. \$25,000
 - d. \$10,000
 - e. \$5,000

Answer: e

18. Which of the following is not a component of the Farm Credit System?
- a. Farm Credit Banks
 - b. Agricultural Credit Associations
 - c. Federal Land Credit Associations
 - d. Farm Credit Administration
 - e. Agricultural Lending Office

Answer: e

19. Which of the following officially designates a bank as insolvent?
- a. Office of the Comptroller of the Currency
 - b. Federal Reserve
 - c. Office of Thrift Supervision
 - d. Office of National Charters
 - e. Resolution Trust Corporation

Answer: a

20. Which of the following is the receiver of a failed depository institution?

- a. Federal Reserve
- b. Federal Deposit Insurance Corporation
- c. Office of the Comptroller of the Currency
- d. Office of Thrift Supervision
- e. Federal Savings and Loan Insurance Corporation

Answer: b

21. The Federal Deposit Insurance Reform Act of 2005 created which of the following?

- a. Bank Insurance Fund
- b. Deposit Insurance Fund
- c. Savings Association Insurance Fund
- d. National Credit Union Shares Insurance Fund
- e. Federal Savings and Loan Insurance Fund

Answer: b

22. Bank regulations:

- a. can prevent bank failures.
- b. can eliminate economic risk for banks.
- c. serve as guidelines for sound operating policies.
- d. guarantee bankers will make sound management decisions.
- e. guarantee bankers act in an ethical manner.

Answer: c

23. Which of the following is not a fundamental function of the Federal Reserve?

- a. Conduct the nation's monetary policy.
- b. Provide an effective payments system.
- c. Regulate banking operations.
- d. Ensure bank profitability.
- e. All of the above are fundamental functions of the Federal Reserve.

Answer: d

24. The Federal Reserve has Reserve Banks and branches in ____ districts across the country.

- a. 10
- b. 12
- c. 14
- d. 16
- e. 18

Answer: b

25. Which of the following is not one of the Fed's monetary policy tools?

- a. Open market operations
- b. Changes in the fed funds rate
- c. Changes in the discount rate
- d. Changes in the required reserve ratio
- e. All of the above are monetary policy tools of the Fed

Answer: b

26. Which of the following is the most flexible of the Fed's tools for implementing monetary policy?

- a. Changes in the fed funds rate
- b. Changes in the required reserve ratio
- c. Changes in the discount rate
- d. Open market operations
- e. Private placements

Answer: d

27. Currently, the Fed sets the discount rate _____ the target fed funds rate.

- a. 1% - 1.5% below
- b. 2% - 2.5% below
- c. 3% - 3.5% above
- d. 2% - 2.5% above
- e. 1% - 1.5% above

Answer: e

28. Which of the following allows depository institutions to borrow for a fixed term against a variety of collateral that is normally accepted for discount window loans?

- a. Term Auction Facility
- b. Term Securities Lending Facility
- c. Primary Dealer Credit Facility
- d. Troubled Asset Relief Program
- e. Housing and Economic Recovery Facility

Answer: a

29. Which of the following loans Treasury securities to primary dealers in exchange for other securities held by the dealers?
- a. Term Auction Facility
 - b. Term Securities Lending Facility
 - c. Primary Dealer Credit Facility
 - d. Troubled Asset Relief Program
 - e. Housing and Economic Recovery Facility

Answer: b

30. Which of the following is an overnight collateralized loan facility that provides loans for up to 120 days to primary dealers in exchange for a broad range of collateral?
- a. Term Auction Facility
 - b. Term Securities Lending Facility
 - c. Primary Dealer Credit Facility
 - d. Troubled Asset Relief Program
 - e. Housing and Economic Recovery Facility

Answer: c

31. Which type of financial institution has seen the largest drop in their share of U.S. financial assets?
- a. Depository institutions
 - b. Mutual funds
 - c. Insurance companies
 - d. Pension plans
 - e. Finance companies

Answer: a

32. Federal Reserve Reg. ____ makes it illegal for any lender to discriminate on the basis of national origin.
- a. AA
 - b. BB
 - c. Z
 - d. C
 - e. B

Answer: e

33. Federal Reserve Reg. ____ requires disclosure of as to why a costumer was denied credit.

- a. AA
- b. BB
- c. Z
- d. C
- e. B

Answer: c

34. Which of the following was a goal of the Depository Institutions Deregulation and Monetary Control Act of 1980?

- a. To reduce the range of banking services offered.
- b. To allow banks to pay market rates on deposits.
- c. To allow banks to make long-term mortgage loans.
- d. To allow banks to offer Money Market Deposit Accounts.
- e. To reduce the number of leveraged buyouts.

Answer: b

35. The _____ authorized money market deposit accounts.

- a. Depository Institutions Act (Garn-St. Germain)
- b. Competitive Equality Banking Act
- c. Financial Institutions Reform, Recovery and Enforcement Act
- d. Federal Deposit Insurance Corporation Improvement Act
- e. Depository Institutions Deregulation and Monetary Control Act

Answer: a

36. The _____ expanded the FDIC's authority for open bank assistance.

- a. Depository Institutions Act (Garn-St. Germain)
- b. Competitive Equality Banking Act
- c. Financial Institutions Reform, Recovery and Enforcement Act
- d. Federal Deposit Insurance Corporation Improvement Act
- e. Depository Institutions Deregulation and Monetary Control Act

Answer: b

37. The _____ created the Office of Thrift Supervision.

- a. Depository Institutions Act (Garn-St. Germain)
- b. Competitive Equality Banking Act
- c. Financial Institutions Reform, Recovery and Enforcement Act
- d. Federal Deposit Insurance Corporation Improvement Act
- e. Depository Institutions Deregulation and Monetary Control Act

Answer: c

38. The _____ mandated that the FDIC take *prompt corrective action* in dealing with bank failures.
- a. Depository Institutions Act (Garn-St. Germain)
 - b. Competitive Equality Banking Act
 - c. Financial Institutions Reform, Recovery and Enforcement Act
 - d. Federal Deposit Insurance Corporation Improvement Act
 - e. Depository Institutions Deregulation and Monetary Control Act

Answer: a

39. FASB 115 requires historical costs to be used for:
- a. trading account securities.
 - b. available-for-sale securities.
 - c. retained earnings.
 - d. held-to-maturity securities.
 - e. net income.

Answer: d

40. The _____ allows adequately capitalized bank holding companies to acquire banks in any state.
- a. Riegle-Neal Interstate Banking and Branching Efficiency Act
 - b. Competitive Equality Banking Act
 - c. Financial Institutions Reform, Recovery and Enforcement Act
 - d. Federal Deposit Insurance Corporation Improvement Act
 - e. Depository Institutions Deregulation and Monetary Control Act

Answer: a

41. The _____ requires disclosure of a bank's privacy policy.
- a. Riegle-Neal Interstate Banking and Branching Efficiency Act
 - b. Gramm-Leach-Bliley Act
 - c. Financial Institutions Reform, Recovery and Enforcement Act
 - d. Federal Deposit Insurance Corporation Improvement Act
 - e. Depository Institutions Deregulation and Monetary Control Act

Answer: b

42. The _____ repealed the Glass-Steagall Act.
- a. Riegle-Neal Interstate Banking and Branching Efficiency Act
 - b. Gramm-Leach-Bliley Act
 - c. Financial Institutions Reform, Recovery and Enforcement Act
 - d. Federal Deposit Insurance Corporation Improvement Act
 - e. Depository Institutions Deregulation and Monetary Control Act

Answer: b

43. The _____ established to Public Company Oversight Board to regulate public accounting firms that audit publicly-traded companies.
- a. Riegle-Neal Interstate Banking and Branching Efficiency Act
 - b. Competitive Equality Banking Act
 - c. Financial Institutions Reform, Recovery and Enforcement Act
 - d. Sarbanes-Oxley Act
 - e. Depository Institutions Deregulation and Monetary Control Act

Answer: d

44. _____ allowed any institution to “truncate” the paper check at any point in the check clearing process.
- a. Riegle-Neal Interstate Banking and Branching Efficiency Act
 - b. Fair and Accurate Credit Transactions Act
 - c. Troubled Asset Relief Program
 - d. Sarbanes-Oxley Act
 - e. Check 21 Act

Answer: e

45. The _____ created a fund originally designed to allow the U.S. Treasury to purchase distressed assets from financial institutions.
- a. Capital Purchase Program
 - b. Foreclosure Prevention Act
 - c. Troubled Asset Relief Program
 - d. Primary Dealer Credit Facility
 - e. Check 21 Act

Answer: c

46. The _____ authorized the Treasury to purchase debt securities issued by the Fannie Mae, Freddie Mac, and the Federal Home Loan Banks and to purchase common stock.
- a. Treasury Emergency Authority Provisions
 - b. Foreclosure Prevention Act
 - c. Troubled Asset Relief Program
 - d. Primary Dealer Credit Facility
 - e. Check 21 Act

Answer: a

47. Which of the following statements is/are correct?

- a. Higher capital requirements often result in a higher cost of capital for banks.
- b. Small banks have greater access to the equity markets than large banks.
- c. Higher capital requirements encourage small banks to consolidate into larger banks.
- d. All of the above are correct.
- e. Only a. and c. are correct.

Answer: e

48. The Helping Families Save Their Homes Act of 2009 included provisions:

- a. intended to prevent mortgage foreclosures.
- b. to enhance the availability of mortgage credit.
- c. to protect renters living in foreclosed homes.
- d. All of the above are correct.
- e. Only a. and b. are correct.

Answer: d

49. The Consumer Financial Protection Bureau was created as part of the:

- a. Hope for Homeowners Act
- b. Dodd-Frank Act
- c. Fair and Accurate Credit Transactions Act
- d. Gramm-Leach-Bliley Act
- e. Sarbanes-Oxley Act

Answer: b

50. The lack of incentive to guard against risk where one is protected from it is known as:

- a. risk aversion
- b. too big to fail
- c. protection guarantee
- d. incentive failure
- e. moral hazard

Answer: e

True/False

51. A dual banking system means that both the federal government and individual states charter banks and credit unions.

Answer: True

52. A *memorandum of understanding* is a legal document that orders a firm to stop an unfair practice.

Answer: False

53. A function of investment banking is to facilitate corporate mergers and acquisitions.

Answer: True

54. Most banks have the ability to easily raise new capital by issuing new equity.

Answer: False

55. Credit union membership is based upon a strict common bond that defines the members.

Answer: False

56. Bank regulations can guarantee that bankers will make sound management decisions.

Answer: False

57. State-chartered banks must be members of the Federal Reserve System.

Answer: False

58. The Dodd-Frank Act eliminates “Too-Big-To-Fail” bailouts.

Answer: True

59. The Federal Reserve serves as the lender of last resort.

Answer: True

60. The FDIC insures credit union accounts up to \$250,000.

Answer: False

Essay

61. Discuss the limits on the types of products and services a commercial bank can offer.

62. Briefly explain the components of the CAMELS system.

63. Discuss why several investment banks choose to become financial holding companies in 2008.

64. Discuss how the degree of regulation is different for depository institutions versus non-depository institutions.

65. Discuss two of the shortcomings of restrictive bank regulation.