
Principles of Banking

Tenth Edition

This publication is designed to provide accurate and authoritative information in regard to the subject matter covered. It is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional service. If legal advice or other expert assistance is required, the services of a competent professional person should be sought.

From a Declaration of Principles jointly adopted by a Committee of the American Bar Association and a Committee of Publishers and Associations

The American Bankers Association is committed to providing innovative, high-quality products and services that are responsive to its members' critical needs.

To comment about this product, or to learn more about the American Bankers Association and the many products and services it offers, please call **1-800-BANKERS** or visit us at our Web site: **www.aba.com**.

This textbook has been approved by the American Institute of Banking for use in courses for which AIB certificates or diplomas are granted. The American Institute of Banking is the professional development and training affiliate of the American Bankers Association. Instructional materials endorsed by AIB have been developed by bankers for bankers.



**American
Institute of
Banking**



American
Bankers
Association

Layout and composition of the *Principles of Banking* textbook was done by Wendi Calvert, Calvert Creative Design (wendeyec@hotmail.com), Punxsutawney, PA.

Editing of the tenth edition was done by Allyn C. ("Allie") Buzzell, Adeptus Associates, Middletown, MD.

© 2010 by the American Bankers Association
Tenth Edition

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means—electronic, mechanical, photocopying, recording, or otherwise—without prior written permission from the American Bankers Association.

Printed in the United States of America
10 9 8 7 6 5 4 3 2 1

Catalog Number: 3005834

ISBN: 0-89982-655-5

Contents

EXHIBIT LIST	XV
PREFACE	XIX
ACKNOWLEDGMENTS	XXV
CHAPTER 1	BANKING AND YOU
LEARNING OBJECTIVES	1
INTRODUCTION	2
THE ROLE OF A BANK EMPLOYEE	3
Service to Customers	3
A Sense of Responsibility	3
Worthy of Trust	3
Professionalism	5
Bank Employee Careers	5
Bank Employee Training	7
THE BANK AS AN ORGANIZATION	7
Typical Bank Structure	8
Bank and Financial Holding Companies	10
BANK PRODUCTS AND SERVICES	11
Traditional Products and Services	12
Nontraditional Products and Services	12
Electronic Services	13
Marketing and Cross-Selling Services	13
THE BANK AND THE COMMUNITY	13
Financial Services	13
Customer Service	14
Contribution to the Economy	14
Community Support	14
PARTNERSHIPS AND OUTSOURCING	15
MERGERS AND ACQUISITIONS	15
FUTURE TRENDS	16
Regulatory Evolution	16
Financial Services Expansion	16
Continued Competition	17
Margin Squeeze	17
Technological Advances	17
Geographic Expansion	17

SUMMARY	18
ENDNOTES	19
SELF-CHECK AND REVIEW	19
ADDITIONAL RESOURCES	19

CHAPTER 2 THE U.S. BANKING SYSTEM

LEARNING OBJECTIVES	21
INTRODUCTION	22
BANKING AND THE ECONOMY	22
U.S. BANKING SYSTEM: 1700s –1913	23
The Early Banking System	23
Failed Attempts to Form a Central Bank	24
Establishing the Federal Reserve System	26
BANKING IN THE 20TH CENTURY	26
The Great Depression and Bank Protections	28
Social Change and Consumer Protection	30
Bank Competition	32
The Savings and Loan Crisis	35
BANKING IN THE 21ST CENTURY	37
Opportunity	38
Financial Privacy and Protecting the Nation	39
Accountability: The Sarbanes-Oxley Act	40
Economic Stabilization and Recovery	40
FEDERAL RESERVE SYSTEM	42
The Fed’s Structure	42
The Fed’s Duties	44
Federal Reserve Services	45
REGULATORS AND REGULATIONS	46
Bank Regulators	46
Bank Regulations	47
SUMMARY	49
SELF-CHECK AND REVIEW	51
ADDITIONAL RESOURCES	51

CHAPTER 3 MONEY AND BANKING

LEARNING OBJECTIVES	53
INTRODUCTION	54
THE EVOLUTION OF MONEY	54
Coin and Currency	54
Fiat Money	56
THE FUNCTIONS AND PROPERTIES OF MONEY	57
Functions of Money	57

Properties of Money	58
Alternatives to Coin and Currency	59
THE MONEY SUPPLY AND THE ECONOMY	60
How the Money Supply Is Measured	61
The Flow of Economic Activity	62
BANKS AND MONEY CREATION	66
Money Creation	66
THE FEDERAL RESERVE AND MONETARY POLICY	68
Reserve Requirements	68
Discount Operations	69
Open Market Operations	70
SUMMARY	71
ENDNOTES	72
SELF-CHECK AND REVIEW	73
ADDITIONAL RESOURCES	73
CHAPTER 4 DEPOSIT ACCOUNTS	
LEARNING OBJECTIVES	75
INTRODUCTION	76
THE DEPOSIT FUNCTION	76
Safety	77
Customer Convenience	77
DEPOSIT ACCOUNT PRODUCTS	77
Types of Deposit Accounts	77
Common Deposit Account Products	79
DEPOSIT-RELATED SERVICES	81
Options for Depositing Funds	81
Types of Deposited Items	83
Accessing Funds and Account Information	84
OWNERSHIP OF DEPOSIT ACCOUNTS	84
Consumer Account Ownership	84
Business Account Ownership	86
OPENING A DEPOSIT ACCOUNT	88
Establishing Identity	89
Evaluating Capacity and Authority	89
DEPOSIT REGULATIONS	90
Reserve Requirements	90
Electronic Funds Transfer	90
Expedited Funds Availability	91
Truth in Savings	91
FDIC Insurance Protection	92
SUMMARY	94

ENDNOTE	95
SELF-CHECK AND REVIEW	95
ADDITIONAL RESOURCES	96
CHAPTER 5	PAYMENTS: CASH AND CHECKS
LEARNING OBJECTIVES	97
INTRODUCTION	98
CASH AS A PAYMENT SYSTEM	98
United States Legal Tender	98
Damaged Coin and Currency	99
CHECKS AS A PAYMENT SYSTEM	100
Uniform Commercial Code	100
Elements of Negotiable Instruments	100
Other Types of Checks	102
THE CHECK PAYMENT PROCESS	103
The Drawer	103
The Payee	105
The Depository Bank	106
The Drawee	111
ELECTRONIC CHECK PROCESSING	113
CHECK FRAUD	115
Check Counterfeiting	115
Closed Account Fraud	115
Check Kiting	116
Bank Efforts to Combat Check Fraud	116
LAWS AND REGULATIONS	117
Collection of Checks and Funds Transfers	117
Expedited Funds Availability Act	117
SUMMARY	118
ENDNOTE	119
SELF-CHECK AND REVIEW	119
ADDITIONAL RESOURCES	119
CHAPTER 6	ELECTRONIC BANKING
LEARNING OBJECTIVES	121
INTRODUCTION	122
THE DEVELOPMENT OF ELECTRONIC BANKING	122
The Roots of Electronic Banking	122
Trends in Electronic Banking	123
PROCESSING ELECTRONIC TRANSACTIONS	125
EFT and ACH	125
Fedwire, CHIPS, and SWIFT	126

Other Federal Reserve Services	128
ELECTRONIC BANKING AND CONSUMERS	128
Bank Web Sites	129
Internet Banking Services	130
Card Access to Funds	133
ELECTRONIC BANKING AND BUSINESS	135
Electronic Bill Presentment and Payment (EBPP)	135
Imaging and Remote Deposit Capture	135
LAWS AND REGULATIONS	136
Electronic Funds Transfers	136
Funds Availability	136
Check Collection and Funds Transfers	137
Check Conversion	137
Electronic Signatures	137
SUMMARY	138
ENDNOTES	139
SELF-CHECK AND REVIEW	139
ADDITIONAL RESOURCES	140

CHAPTER 7 LENDING

LEARNING OBJECTIVES	141
INTRODUCTION	142
THE LENDING FUNCTION	142
Sources of Credit	142
Banks as Lenders	143
LOAN CATEGORIES	143
Consumer Loans	143
Real Estate Loans	145
Business Loans	146
Government and Government-Sponsored Loans	149
THE LENDING PROCESS	150
The Application and Interview	150
The Investigation	152
Loan Documentation	154
Loan Decision	155
Loan Administration	155
Loan Review and Asset Recovery	156
LOAN POLICY	157
LAWS AND REGULATIONS	157
Equal Credit Opportunity Act	158
Truth in Lending Act	159
Community Reinvestment Act	159

Loans to Bank Insiders	160
Home Mortgage Disclosure Act	160
Real Estate Settlement Procedures Act	160
Fair Credit Reporting Act	160
Flood Disaster Protection Act	161
Bank Lending Limits	161
SUMMARY	161
ENDNOTE	162
SELF-CHECK AND REVIEW	163
ADDITIONAL RESOURCES	163

CHAPTER 8 **PERSONAL FINANCIAL PLANNING**

LEARNING OBJECTIVES	165
INTRODUCTION	166
FINANCIAL HEALTH EQUALS PERSONAL WEALTH	166
Banks and Financial Planning	168
Financial Planning Goals	168
Time Value of Money	168
Risk Management Considerations	169
The Role of the Planner	170
Ethical Standards	170
Minimizing Tax Liability	170
FINANCIAL PLANNING PROCESS	171
Customer Life Stages	171
Financial Planning Goals	172
Financial Services Products	173
Net Worth Statement	173
Cash Flow Strategy	175
INSURANCE PROTECTION	175
Life Insurance	176
Health, Disability, and Long-term Care Insurance	177
Property, Title, and Vehicle Insurance	178
Liability Insurance	178
INVESTMENT SERVICES	179
Investment Strategies	179
Portfolio Management	181
RETIREMENT PLANNING	182
Social Security and Pensions	183
Individual Retirement Accounts	184
Estate Planning	186
TRUST SERVICES	187
Estate Settlement	188

Trust Administration	189
Guardianship	189
Personal Agency Services	190
LAWS AND REGULATIONS	190
Retail Sales of Nondeposit Investment Products	191
Consumer Protection in Sales of Insurance	191
Heroes Earned Retirement Opportunities	191
Uniform Laws	191
SUMMARY	192
ENDNOTES	194
SELF-CHECK AND REVIEW	194
ADDITIONAL RESOURCES	195

CHAPTER 9 BUSINESS AND INTERNATIONAL BANKING SERVICES

LEARNING OBJECTIVES	199
INTRODUCTION	200
BUSINESS BANKING SERVICES	200
Cash Management	200
Other Business Banking Products and Services	204
Capital Markets	205
BUSINESS TRUST SERVICES	206
Corporate Agency Services	207
Employee Benefit Services	208
INTERNATIONAL BANKING	212
International Payments	214
Foreign Exchange Services	215
LAWS AND REGULATIONS	215
Fiduciary Activities of National Banks, Regulation 9	216
Gramm-Leach-Bliley Act	216
Uniform Commercial Code Article 5	217
Federal Reserve Regulation K	
(International Operations of U.S. Banking Organizations)	217
SUMMARY	218
ENDNOTES	219
SELF-CHECK AND REVIEW	219
ADDITIONAL RESOURCES	220

CHAPTER 10 BANK INVESTMENTS AND PERFORMANCE

LEARNING OBJECTIVES	221
INTRODUCTION	222
THE ANNUAL REPORT	222
Statement of Condition	223

Profit and Loss Statement	225
Statement of Cash Flows	227
IMPORTANCE OF FINANCIAL INFORMATION	227
Shareholders and Investors	227
Regulators	228
Other Banks	228
Customers	228
Employees	228
MANAGEMENT OF BANK FUNDS	228
Business Risks in Banking	229
Asset and Liability Management	229
FUNDS MANAGEMENT OBJECTIVES	230
Liquidity	230
Safety	231
Income	232
MAXIMIZING ASSET RETURN	232
Loans Vs. Investments	232
Credit Risk Vs. Market Risk	233
Loan Interest	233
Market Interest Rates and Lending	234
Investment Diversification	235
Investment Requirements	235
Types of Bank Investments	235
Fee Income	237
PERFORMANCE MEASURES	238
Financial Ratios	238
Other Performance Measures	240
BUDGETING AND PLANNING	241
The Budgeting Process	241
Budget Variances	241
LAWS AND REGULATIONS	242
Generally Accepted Accounting Principles	242
Regulatory Reporting	242
SUMMARY	244
SELF-CHECK AND REVIEW	246
ADDITIONAL RESOURCES	247
CHAPTER 11	BUILDING RELATIONSHIPS: SALES, MARKETING, AND CUSTOMER SERVICE
LEARNING OBJECTIVES	249
INTRODUCTION	250
SELLING TODAY	250

Sales, Marketing, and Customer Service	250
The Market-Driven Strategy	251
MEETING CUSTOMER EXPECTATIONS	253
Responsive Service and Problem Resolution	254
Competent Staff	254
Customer Perspective	254
Courteous Treatment	255
Reliable Services	255
Viable Products and Services	256
Professional Appearance	256
Access to Funds and Staff	256
Financial Privacy	257
CROSS-SELLING AND REFERRALS	257
THE PURCHASING PROCESS	258
Needs Identification	258
Prepurchase Searching	259
Purchase Decision	260
Postpurchase Assessment	260
PRODUCT DEVELOPMENT	260
LAWS AND REGULATIONS	263
FDIC Insurance Notification	264
Unfair or Deceptive Acts or Practices	264
Do Not Call, Do Not Fax	265
CAN-SPAM Act	266
Prescreening	267
SUMMARY	267
ENDNOTES	269
SELF-CHECK AND REVIEW	269
ADDITIONAL RESOURCES	269

CHAPTER 12 **SAFEGUARDING CUSTOMER INFORMATION**

LEARNING OBJECTIVES	271
INTRODUCTION	272
PROTECTING CUSTOMER INFORMATION	272
Data Security	272
General Security Features	273
Emergency Preparedness	274
CUSTOMER IDENTIFICATION	274
Account Identification Requirements	274
Account Access Identification Methods	275
Passwords	275
Biometric Identification Methods	276

FRAUD AND PREVENTION METHODS	277
Caller-ID Manipulation	278
Pretext Calling	278
Online Fraud Schemes	278
Computer Attacks	280
Laptop Computer Theft	282
Wireless Hacking	283
Bank Card Fraud	284
Elder Financial Abuse	285
Identity Theft	286
WHAT CUSTOMERS CAN DO	288
Communication Devices	288
Computers	289
Credit Reports	289
LAWS AND REGULATIONS	290
Privacy of Consumer Financial Information	290
Interagency Guidelines on Information Security	290
Interagency Guidance on Internet Authentication	291
Protecting Children Online	291
Right to Financial Privacy	291
State Requirements Protecting Social Security Numbers	291
Red Flag Rules	292
SUMMARY	292
SELF-CHECK AND REVIEW	293
ADDITIONAL RESOURCES	293
CHAPTER 13	SAFEGUARDING THE BANK, THE ECONOMY, AND THE NATION
LEARNING OBJECTIVES	295
INTRODUCTION	296
MANAGING RISK	296
Uniform Ratings Systems	296
Enterprise Risk Management	298
SAFEGUARDING BANK ASSETS	298
Corporate Governance and Ethical Behavior	298
Employee Hiring and Vendor Management	300
Crimes Against Banks	303
SAFEGUARDING THE ECONOMY AND THE NATION	309
Terrorism	310
Emergency Preparedness	313
SUMMARY	316

SELF-CHECK AND REVIEW	317
ADDITIONAL RESOURCES	317
ANSWERS TO SELF-CHECK AND REVIEW	
Chapter 1	319
Chapter 2	320
Chapter 3	321
Chapter 4	324
Chapter 5	326
Chapter 6	328
Chapter 7	329
Chapter 8	331
Chapter 9	333
Chapter 10	335
Chapter 11	337
Chapter 12	339
Chapter 13	341
GLOSSARY	343
INDEX	359

Exhibit List

CHAPTER 1

Exhibit 1.1	Sample Careers in Banking and Education Qualifications	5
Exhibit 1.2	Sample Certifications Through the Institute of Certified Bankers	6
Exhibit 1.3	Types of Financial Institutions	7
Exhibit 1.4	Typical Commercial Bank Organization	8
Exhibit 1.5	Sample Bank Holding Company Activities	10
Exhibit 1.6	Sample Financial Holding Company Activities	11
Exhibit 1.7	A Hypothetical Financial Holding Company Organizational Chart	12
Exhibit 1.8	Bank Mergers, Charters, and Failures	15

CHAPTER 2

Exhibit 2.1	Milestones in the Evolution of U.S. Banking	23
Exhibit 2.2	Timeline of Banking Legislation in the 20th Century	28
Exhibit 2.3	Innovations in Banking in the 20th and 21st Centuries	31
Exhibit 2.4	Consumer Protection Laws	32
Exhibit 2.5	Number of Bank Failures, 1934-2009	36
Exhibit 2.6	Timeline of Banking Legislation in the 21st Century	37
Exhibit 2.7	Chronology of Major Banking Legislation and Events	43
Exhibit 2.8	Structure of the Federal Reserve System	44
Exhibit 2.9	Categories of Federal Reserve Regulations	48

CHAPTER 3

Exhibit 3.1	Components of the Money Supply	61
Exhibit 3.2	The Circular Flow of Economic Activity	63
Exhibit 3.3	U.S. Balance of Trade and the Economy	65
Exhibit 3.4	Banks and Multiple Deposit Creation	67
Exhibit 3.5	Federal Reserve Tools and Their Effects	69
Exhibit 3.6	Composition of the Federal Open Market Committee	70

CHAPTER 4

Exhibit 4.1	A Bank's Relationship with Depositor and Borrower	76
Exhibit 4.2	Characteristics of Deposited Items	83
Exhibit 4.3	Account Ownership	84
Exhibit 4.4	FDIC's Deposit Insurance Ownership Categories and Coverage	93

CHAPTER 5

Exhibit 5.1	U.S. Cash Distribution System	99
Exhibit 5.2	Parties to a Check	100

Exhibit 5.3	Elements of a Negotiable Check	101
Exhibit 5.4	Check Payment Process	103
Exhibit 5.5	Visual and Nonvisual Tests for Inspecting a Check	106
Exhibit 5.6	Presenting Checks for Payment and Posting	108
Exhibit 5.7	Magnetic Ink Character Recognition (MICR) Line	109
Exhibit 5.8	Check Sorting and Bundling	110
Exhibit 5.9	Recognizing Substitute Checks	114
Exhibit 5.10	Check 21 Conversion Process	115
CHAPTER 6		
Exhibit 6.1	Process Flow for Preauthorization Payment	126
Exhibit 6.2	CHIPS Members' Countries	127
Exhibit 6.3	Consumer Banking Preferences	129
Exhibit 6.4	Banking Services Commonly Available Online	130
Exhibit 6.5	Debit Card Point-of-Sale Transactions	134
CHAPTER 7		
Exhibit 7.1	Consumer Loan Pricing Methods	146
Exhibit 7.2	The Lending Process	151
Exhibit 7.3	Sample Loan Interview Questions	151
Exhibit 7.4	The Five Cs of Credit	152
CHAPTER 8		
Exhibit 8.1	Personal Savings Rate in the United States	167
Exhibit 8.2	The Risk Pyramid	169
Exhibit 8.3	Net Worth Worksheet	174
Exhibit 8.4	Monthly Cash Flow Plan for a Single Working Person	176
Exhibit 8.5	Trends in Defined Benefit and Defined Contribution Plans	184
Exhibit 8.6	Traditional IRA Vs. Roth IRA	185
CHAPTER 9		
Exhibit 9.1	Cash Concentration	203
Exhibit 9.2	Corporate Trust Chain of Events for a Bond Offering	207
Exhibit 9.3	Qualified Plan Requirements	210
CHAPTER 10		
Exhibit 10.1	Consolidated Statement of Condition	223
Exhibit 10.2	Consolidated Profit-and-Loss Statement	226
Exhibit 10.3	Banking Industry Statement of Cash Flows (billions of dollars)	227
Exhibit 10.4	Risk Areas in Banking	229
Exhibit 10.5	Comparison of Selected Interest Rates: 1964-2009	235
Exhibit 10.6	Sources of Fee Income	238
Exhibit 10.7	Financial Ratios for FDIC-Insured Institutions 2009	239
Exhibit 10.8	Banking Industry ROA and ROE	240

CHAPTER 11		
Exhibit 11.1	The Purchasing Process	258
Exhibit 11.2	New Product Development	261
CHAPTER 12		
Exhibit 12.1	A Rogue’s Gallery of Malware	281
Exhibit 12.2	Laptop Computer Security Safeguards for Bank Employees	283
CHAPTER 13		
Exhibit 13.1	Contents of a Typical Bank Code of Conduct	301
Exhibit 13.2	Outsourcing Services—Vendor Management	303
Exhibit 13.3	Bank Robbery Response Tips	305
Exhibit 13.4	The Redesigned \$5 Bill	306
Exhibit 13.5	Know Your Money—Raised Banknote	307
Exhibit 13.6	Suspicious Package Poster	311

Preface

Principles of Banking is an entry-level textbook intended to give those who are new to banking a general understanding of banking today. *Principles of Banking* introduces fundamental banking concepts and principles, the basics of how banks operate as a business, their obligation to operate in a safe and sound manner and manage risks, and the responsibilities of bank employees in a customer-focused financial services environment.

OBJECTIVES OF THIS BOOK

- Explain the context, structure, and operation of banks as profit-making enterprises that rely on employees to provide customer-focused service.
- Describe how the evolution of the U.S. banking system has led to opportunities and responsibilities for banks and bank employees today.
- Explain what money is and how it evolved, what constitutes the money supply, the flow of economic activity, and how the Federal Reserve affects monetary policy.
- Describe deposit products and services, the bank's function in opening deposit accounts, and laws and regulations relating to deposits.
- Describe the care and distribution of coin and currency, components of checks as negotiable instruments, types of endorsements, the check payment process, and check fraud schemes.
- Explain banking laws and regulations related to payment processes.
- Discuss how consumers and businesses bank electronically, how electronic banking is evolving, and laws relating to electronic banking.
- Identify the types of loans banks offer their customers, the lending process, and laws and regulations pertaining to lending.
- Describe what constitutes personal financial planning; the insurance, investment, retirement, and trust products and services banks offer to support their customers' financial plans; and how such services are regulated.
- Describe the specialized cash management, insurance, capital markets, trust, employee benefit, and international banking services banks offer to meet the financial needs of their business customers.
- Identify the financial statements that banks use and explain banks' business operations, from managing assets and liabilities to maximizing returns on loans and investments, as well as minimizing expenses and risks, monitoring financial performance, and planning for the future.
- Explain how banks build relationships with customers by meeting their expectations, what factors influence their purchasing decisions, and how both banks and their customers benefit from effective sales and marketing practices.
- Identify methods by which banks protect customer data, identify customers, and authenticate transactions; and describe the various types of fraud against bank customers and how they can protect their privacy.

- Explain the rating systems regulators use in evaluating bank safety and soundness; and describe the roles of boards of directors, management and board committees, officers, and employees in safeguarding bank assets.
- Explain how banks safeguard their assets and protect the nation's economy by adopting appropriate employee hiring and vendor management practices and remaining vigilant to crimes against banks.

INSTRUCTIONAL DESIGN FEATURES

This tenth edition of *Principles of Banking* again contains 13 chapters to better accommodate an instructional schedule for a 10- or 16-week course. As before, the text is typeset in a single column and features sidebars that highlight particularly interesting information. Graphics and color visually enhance the reading and learning experience. Other notable instructional design features include

- learning objectives at the beginning of the chapters
- chapter introductions that set the stage for topics covered in each chapter
- sidebars, charts, illustrations, exhibits, “By the Numbers,” and “Did You Know?” callouts that supplement chapter content
- definitions in sidebars for terms bolded in the text
- situations that illustrate concepts
- banker profiles that describe banking career and education possibilities
- customer tips related to certain chapter topics
- summaries that review each chapter's main points
- self-check and review questions for testing comprehension
- additional resources, such as publications and Web sites, that provide material related to chapter content
- answers to chapter self-check and review questions in a separate section at the back of the book
- a glossary that defines terms used in the text
- an index to assist with the location of content

CHANGES TO THIS EDITION

The tenth edition of *Principles of Banking* contains updated information throughout. You will find new information on such topics as:

- Overall banking trends in such areas as regulatory evolution, financial services expansion, intensified competition, and technological advances.
- U.S. banking system development and growth, including how the banking industry was affected by the recession of 2008-2009.
- Risky lending and investment practices, including the consequences of subprime lending, ill-advised investment practices, and speculation in mortgage-backed securities for financial institutions and the U.S. economy as a whole.
- New financial legislation, including the Emergency Economic Stabilization Act of 2008 and the Credit Card Accountability, Responsibility and Disclosure (CARD) Act of 2009.
- Deposit account products, including education savings and health savings accounts.

- New FDIC insurance coverage rules and the temporary increase in maximum insurance coverage to help stabilize the economy and protect depositors.
- Electronic banking developments, such as the growing consumer preference for wireless devices, including mobile phones and personal digital assistants, to perform financial transactions.
- New consumer and business loan products such as reverse mortgages.
- Recent regulatory and legislative actions that affect banking, including action taken to revitalize the economy by encouraging lending.
- Updated information on insurance, investment, and retirement products for bank customers.
- Bank corporate governance and financial reporting responsibilities.
- Laws and regulations that govern bank advertising and sales practices.
- Improved methods for securing bank information, including multifactor authentication and biometric identification.
- Recent developments in computer security attacks, including laptop computer theft, wireless hacking, and bank card fraud.
- New laws and regulations to deter threats to customer information and bank security systems.
- Ways the government and banks are safeguarding the nation's financial assets, such as new currency security features, antiterrorism response measures, and natural disaster and pandemic preparedness.

Exhibits have also been updated and new exhibits added to illustrate and clarify new material.

CONTENT OVERVIEW

Principles of Banking begins with an introduction to the general responsibilities of bank employees and the bank to customers, the bank's shareholders, and the community in which the bank operates. Chapter 1 also explains how bank employees serve customers in many capacities and are accountable to the bank and their fellow employees. In addition, bank employees must adhere to the bank's policies and procedures. To better serve their customers, banks continually seek ways to improve their products and services and take advantage of new opportunities.

Chapter 2 covers the big picture—the role of banking in the U.S. economy. It looks at how the U.S. banking system evolved, the events and factors driving banking-related legislation, and the opportunities and responsibilities of banks in the twenty-first century as they already have been shaped by economic uncertainty and technological advances. This chapter gives a context for understanding how providing customers with financial products and services is an important function in the larger business, economic, and social system.

Money—which is at the heart of banking—also has evolved over time. The value of money is important for an economy's growth and stability. Chapter 3 explores banks' critical role in helping to create money and fulfill the Federal Reserve's duty to control the money supply and keep the U.S. economy stable.

The deposit account, a core bank product, is the subject of Chapter 4. Checking, savings, money market, and time deposit accounts are discussed in this chapter, as are the different ways bank customers can deposit funds. The type of deposit account a customer opens and the way the account is titled determines account ownership, which in turn has a bearing on account opening procedures.

Bank customers not only make deposits, they also move money out of their accounts to make payments. Chapter 5 looks at cash and checks as payment systems. This chapter especially focuses on the check payment function. Whether a customer is paying for products and services or cashing a check at the teller window, it is important to know how the check is processed through the clearing system and eventually charged to the paying bank for debit to the account of the check writer. The chapter also covers legal requirements for paper and electronic checks as negotiable instruments.

Cash and paper checks have been used for centuries, but advancements in electronic banking may soon relegate them to a secondary role. Chapter 6 explores how electronic transactions are processed and the new ways banking is being done electronically by consumers and businesses through such channels as virtual banks, mobile banking, and contactless payment devices.

Chapter 7 covers consumer and business lending—a traditional core banking function. The chapter looks at the many consumer and commercial loan products that are marketed and examines each stage of the lending process from loan application to loan administration and review.

Although banks once simply offered checking and savings accounts and made loans, they now seek to meet the total financial needs of their customers. Chapter 8 explores the basics of crafting a personal financial plan for bank customers, and the bank products and services, such as insurance products, investments, retirement vehicles, and trust services, that are available to consumers to achieve the goals of those plans.

The subject of Chapter 9 is the financial products and services banks provide to their business customers. Cash management, insurance, capital markets products, trust services, and international banking—a business that is growing along with global commerce—help businesses of all sizes fulfill their strategic and operational goals.

In supplying essential products and services to customers, banks amass assets and liabilities and must manage them to produce a profit for shareholders. Chapter 10 looks at how banks operate as a business and how their performance is reflected in financial reports that show where and how the bank acquired funds, how the funds were put to work, and the results achieved.

Another key to bank profitability and success is building long-term customer relationships. Chapter 11 looks at how banks strive to provide excellent customer service and create and sell products and services that meet customers' needs and expectations.

The text concludes by considering the stewardship responsibilities of banks. Banks have a special duty to protect customer information, safeguard customer and bank assets, deter financial crimes, combat computer attacks, and help protect the

nation's financial system against misuse and corruption. That is why banking has been called a "public trust." Chapter 12 looks at these issues in terms of protecting customer information and assets.

Chapter 13 continues the theme of stewardship by exploring how the safety and soundness of banks are ensured through regulatory oversight and by risk management techniques that deter threats from within—for example, unethical or irresponsible employee behavior—and from without—for example, robbery, counterfeiting, and fraud. The chapter also addresses the special and unique role that banks play in thwarting terrorism and helping the nation and economy recover from disasters, both natural and man-made.

Acknowledgments

The American Bankers Association extends its gratitude to Nancy Derr-Castiglione who was subject matter expert reviewer for this edition. Ms. Derr-Castiglione (Nancy D-C for short) is an ICB Certified Regulatory Compliance Manager. She is the President and owner of D-C Compliance Services, a regulatory compliance consulting services firm that was founded in 2002 to provide expertise in compliance training, monitoring, risk assessment, and development of compliance policies and processes to a wide range of financial institution clients. Nancy has been working in the field of bank compliance for over 30 years, starting out as an assistant national bank examiner with the Office of the Comptroller of the Currency. She has been actively involved with the American Bankers Association and has served on the ABA Compliance Executive Committee, the National and Graduate Compliance Schools Board, and the Editorial Advisory Board of the *ABA Bank Compliance* magazine. In 2001, Nancy was the recipient of the ABA's Distinguished Service Award for service to the regulatory compliance management profession. She is currently a contributing editor for the *ABA Banking Journal*.

The American Bankers Association also wishes to thank David Buzzell for updating the tenth edition of *Principles of Banking*. Mr. Buzzell is a writer who specializes in banking and business topics and has served as an author for several ABA textbooks and other publications. Mr. Buzzell is a principal in Adeptus Associates in Middletown, MD.

Janita Ponze and Sally Spasovski shared the project manager role for the tenth edition. Janita Ponze initiated the update of the tenth edition and retired after many years of service to ABA publications. Sally Spasovski, MBA, MEd, is a training consultant who has worked with the ABA since 2000. Ms. Spasovski was co-author of the eighth edition of *Principles of Banking* and has collaborated with the ABA on many of its course offerings. Sally is located in Tempe, AZ.

The American Bankers Association also extends sincere thanks to the task force members who reviewed and commented on the previous edition or the manuscript of this textbook. They provided valuable guidance on both content and presentation.

Michelle Allen, CFMP
Vice President
Marketing Director
Community Trust Bank
Ruston, Louisiana

Ken Blendea, CFSSP
Assistant Vice President
Security Officer
National Bank and Trust
Wilmington, Ohio

David M. Eldred, CFMP
Senior Vice President
Marketing & Product
Management
Liberty Bank
Eugene, Oregon

Richard E. Beck, Jr.
Senior Vice President
Corporate Sales Manager
STAR Financial Bank
Fort Wayne, Indiana

Rita Buchholz, CTFA
Trust Officer
Northwestern Mutual Wealth
Management Company
Milwaukee, Wisconsin

G. Jay Francis
Senior Vice President
Director of Operational
Risk Management
Univest Corporation
of Pennsylvania
Souderton, Pennsylvania

Salli M. Goodrow
Senior Platform
Training Officer
Fulton Financial Corporation
Lancaster, Pennsylvania

Jon A. Hooks, Ph.D., CFA
Professor of Economics
and Management
Albion College
Albion, Michigan

Karen S. Schellin, CFSSP
Vice President
Fraud Manager
First Banking Center
Kenosha, Wisconsin

Zach Grimes, CPA, CTFA
First Vice President
Senior Product Manager
Robert W. Baird & Co.
Milwaukee, Wisconsin

Debra A. Lurgio
Assistant Vice President and
Assistant Controller
ShoreBank
Chicago, Illinois

Kevin J. Thiele
Vice President and
Member, Board of Directors
Wahoo State Bank
Wahoo, Nebraska