Major Financial Laws: Banking and Payments Laws

Center Forward Basics

December 2025

The Financial Services industry is subject to a web of regulations and laws across federal and state jurisdictions. The regulatory environment can thus be confusing, especially given the overlapping powers and jurisdictions that often define the industry. This Basic is the first in a new financial services series in which we will dive into reviews of the regulatory environment to demystify the laws and regulations of the Financial Services industry. This first Basic will discuss the major laws governing banking and payments in the United States.

The laws governing banking and payments in the United States are among the oldest financial regulations in the U.S.. At the country's founding, most banking laws were enacted at the state level. However, during and after the Civil War, the federal government began to legislate the banking industry. Soon afterwards, U.S. payment regulations began to appear, most of which were implemented in the mid-twentieth century. After a century and a half, U.S. banking and payment legislation has created a robust set of regulations that have strengthened the U.S. financial services industry and supported the U.S. economy. Banking legislation focuses primarily on prudential regulations, and the agencies that oversee it primarily have supervisory roles. This means the laws focus on the solvency and stability of banking institutions, with supervisors ensuring the safety and soundness of the institutions they supervise. Payments legislation has trended toward fraud prevention and encouraging anti-discriminatory behavior. This does not mean that most major banking and payments legislation has not overlapped. Both, to some degree, encourage resilient financial institutions and discourage fraud and discrimination. However, as the U.S. continues to evolve and add more regulations, legislators need to carefully strike a balance between encouraging innovation and economic growth and ensuring a robust banking and payments infrastructure, a balance they have been considering since the first banking and payments laws were implemented in the mid-nineteenth century.

Center Forward Basics

Center Forward brings together members of Congress, not-for profits, academic experts, trade associations, corporations and unions to find common ground. Our mission: to give centrist allies the information they need to craft common sense solutions, and provide those allies the support they need to turn those ideas into results.

In order to meet our challenges we need to put aside the partisan bickering that has gridlocked Washington and come together to find common sense solutions.

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National Bank Act of 1863 and 1864

The National Bank Acts, passed during the Civil War, were some of the first pieces of federal banking legislation. Primarily, these acts established the dual banking system, where both state and national banks coexist, and established the Office of the Comptroller of the Currency, which charters and supervises national banks.

Federal Reserve Act of 1913

This legislation created the Federal Reserve System, which consists of 12 regional Federal Reserve Banks and a seven-member Federal Reserve Board of Governors. The Federal Reserve Board of Governors is situated in Washington, D.C., and oversees the Federal Reserve System. The act also created the Federal Reserve's (the Fed's) "dual mandate." The dual mandate requires the Fed to maintain both price stability and maximum employment. Additionally, this act required the Fed to set bank reserve requirements, cash that a bank is required to keep in its vault or at its nearest Federal Reserve Bank, through Regulation D. Lastly, this act requires national banks to be members of the Federal Reserve System, which also means the Fed has supervisory power over national banks.

Banking Act of 1933

Also known as the Glass-Steagall Act, the Banking Act of 1933 was enacted during the Great Depression and overhauled U.S. banking regulations. However, as the U.S. economy evolved, much of this law was overturned at the end of the 20th century with the enactment of the Gramm-Leach-Bliley Act (GLBA). For example, one of the more well-known provisions of the Glass-Steagall Act separated commercial and investment banking. Commercial banks, which were deposit-taking institutions that lent money, were no longer able to engage in underwriting and securities activity, which became the sole purview of investment banks. Overturning this provision was one of the changes made by the Gramm-Leach-Bliley Act (GLBA).

However, some provisions of this legislation remain in effect. For example, the Federal Reserve was given greater supervisory powers, and the Federal Open Market Committee (FOMC), which is the Fed committee responsible for executing monetary policy through purchases of U.S. government securities, was created. In addition, the Glass-Steagall Act created the Federal Deposit Insurance Corporation (FDIC), albeit temporarily, with the Banking Act of 1935 making the FDIC permanent. The FDIC currently insures bank clients' deposits up to a limit (currently $250,000) through bank funding.

Federal Credit Union Act of 1934

The Federal Credit Union Act (FCUA) established the federal credit union system and created a national framework for credit unions. Credit unions are member-owned, not-for-profit financial cooperatives. Enacted during the Great Depression to help expand access to credit, the act authorized the chartering of federal credit unions, defined membership requirements for credit unions, and outlined core authorities such as accepting deposits, making consumer loans, and promoting thrift among members. It also set basic governance standards, including board responsibilities, lending policies, and operational requirements.

Federal credit union oversight was originally handled by the Bureau of Federal Credit Unions, later replaced by the National Credit Union Administration (NCUA) in 1970. Also in 1970, Congress created the National Credit Union Share Insurance Fund (NCUSIF), which insures credit union member deposits up to $250,000, similar to FDIC coverage for banks. Congress has updated the FCUA over time, most notably through the Credit Union Membership Access Act of 1998 (CUMAA), which clarified membership rules and chartering rules surrounding membership, along with strengthening safety-and-soundness requirements.

Bank Holding Company Act of 1956

While this was not the first law to recognize bank holding companies, it redefined what a bank holding company (BHC) is and granted the Fed greater oversight authority over BHCs. This legislation defined a BHC as a corporation with a 25% or greater stake in two or more banks. A stake was also defined as the ability to control or vote on shares. The act also required BHCs to register with the Fed, submitting them to the Fed's supervisory authority. Lastly, all banks were required to divest from nonbanking businesses such as commercial or industrial firms. This is to ensure that no commercial or industrial entity gains an unfair advantage from partnering with a financing entity. The Fed, however, can approve new activities for banks to engage in that it deems not in violation of the nonbanking restriction.

Fair Housing Act

This act, known as the FHA, prohibits discrimination for any housing-related activities based on race, color, religion, national origin, disability, family status, or sex. While the protected classes were more limited when this legislation was passed in 1968, the list above includes the protected characteristics later introduced through subsequent legislation.

Truth in Lending Act of 1968

This legislation, known as TILA or the Consumer Credit Protection Act, requires disclosures of credit terms and conditions in consumer credit transactions. This act also regulates the advertising of credit and certain credit card practices. Additionally, borrowers are granted specific rights on updated disclosures, billing errors, and the treatment of credit balances.

Bank Secrecy Act of 1970

Also known as the Currency and Foreign Transactions Reporting Act, this legislation was created to help combat money laundering by requiring U.S. financial institutions to work with the U.S. government in cases where there is the potential for money laundering, terrorist financing, or fraud. The law creates a framework for anti-money laundering programs and reporting requirements for suspicious information. The act also imposes customer identification, risk assessment, customer due diligence, and record maintenance requirements on financial institutions.

Fair Credit Reporting Act of 1970

The Fair Credit Reporting Act (FCRA) establishes a framework for the use and sharing of consumer reports. It restricts how non-public personally identifiable information can be shared with third parties. Each covered entity is also required to implement an identity theft prevention program.

Home Mortgage Disclosure Act of 1975

Also known as HMDA, this act requires lenders to collect, report, and publicly disclose loan-level information about mortgages. The public HMDA information is used to determine whether lenders are properly serving a community, to allow public officials to make better-informed decisions, and to potentially expose discriminatory lending practices.

Equal Credit Opportunity Act of 1974 and 1976

The Equal Credit Opportunity Act (ECOA) bars discrimination by creditors based on race, color, religion, national origin, sex, marital status, age, applicants deriving income from public assistance programs, or applicants utilizing the Consumer Credit Protection Act or any state law to assert their rights. Creditors are also required to notify all applicants in writing that copies of their appraisals will be delivered promptly, and then must deliver the appraisal promptly.

Fair Debt Collection Practices Act of 1977

This act, known as the FDCPA, created legal protections against abusive debt collection protections for consumers and provided consumers with the ability to revise and validate their debt information. The act gave the Federal Trade Commission (FTC) authority to enforce these regulations on nonbank, 3rd party debt collectors.

Electronic Funds Transfer Act of 1978

The act was designed to establish and expand consumer rights when using electronic fund transfers (EFT) to move money in or out of their bank accounts. An EFT is any electronic transfer of money, such as debit transactions, P2P payments, ATM withdrawals, or ACH transfers. EFTs are generally slower than bank wires but are more cost-effective. The legislation defines the rights, liabilities, and responsibilities of consumers and financial institutions involved in an EFT.

Financial Institutions Reform, Recovery, and Enforcement Act of 1989

Known as the FIRREA, this legislation was passed in response to the Savings & Loan Crisis of the 1980s, attempting to restore trust in the savings and loan industry. FIRREA abolished the Federal Savings and Loan Insurance Corporation (FSLIC), giving the FDIC responsibility for deposit insurance of thrift banks, otherwise known as savings and loans associations. Thrift banks generally offer more limited banking services, focus primarily on home lending, but may offer slightly higher yields on savings accounts. FIRREA also abolished the Federal Home Loan Bank Board, creating the Federal Housing Finance Board (FHFB) and the Office of Thrift Supervision (OTS) in its wake. However, the responsibilities of the FHFB and the OTS were folded into different agencies following the Global Financial Crisis of 2008.

Telephone Consumer Protection Act of 1991 and the Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003

The Telephone Consumer Protection Act (TCPA) regulates the use of calls, text messages, and faxes for marketing purposes. TCPA aims to protect consumer privacy. The Controlling the Assault of Non-Solicited Pornography and Marketing Act (CAN-SPAM) similarly sets up rules surrounding marketing when using emails for commercial purposes.

Riegle Community Development and Regulatory Improvement Act of 1994

This legislation created the Community Development Financial Institutions (CDFI) Fund. The CDFI Fund provides capital and technical assistance to CDFIs and is administered by the U.S. Treasury Department. Additionally, the act works to address "reverse redlining," which is when non-banks target certain underprivileged individuals for abusive loan terms.

Gramm-Leach-Bliley Act of 1999

The Gramm-Leach-Bliley Act (GLBA), also known as the Financial Services Modernization Act, repealed most of what remained of the Glass-Steagall Act. Most consequentially, investment and commercial banks could once again be combined into a single enterprise. GLBA also created the Financial Holding Company (FHC) in a similar vein to the BHC. FHCs are allowed to conduct any financial or financial-related activity, provided such activity is approved by the Fed in consultation with the Treasury. This meant that large institutions could now engage in traditional banking activities, such as deposit-taking and lending, and in more conventional investing services, such as brokerage and securities underwriting. The GLBA requires "functional" regulation of securities and other activities conducted by bank affiliates, which means that brokerage and underwriting services, for example, must be conducted through SEC-registered broker-dealer affiliates. The Fed was given the authority to regulate FHCs, and restrictions were introduced to prohibit the banking arm of an FHC from promoting certain service products of its investment business. The act also allowed national banks for the first time to underwrite municipal bonds and engage in private placements.

Additionally, the GLBA made changes to the Federal Home Loan Bank (FHLB) System, such as reducing barriers to commercial banks' entry into the FHLB System, and preserved state insurance regulation. Lastly, GLBA enacted new, more stringent standards safeguarding consumer privacy and information. The law requires financial institutions to notify consumers about information sharing with third-party affiliates and, in certain circumstances, to give consumers the right to restrict a financial institution from sharing their data. In addition to these information-sharing disclosures, the act also requires financial institutions to safeguard sensitive customer data.

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010

This law, referred to as Dodd-Frank, was the largest overhaul of the financial system since the Great Depression. The act aimed to promote the financial stability of the U.S. and outlaw unfair, deceptive, or abusive business acts or practices (UDAAP). The legislation implemented new banking, payments, and securities regulations (the securities regulations component of Dodd-Frank will be discussed in the next Basic of this series).

Dodd-Frank established the Consumer Financial Protection Bureau (CFPB) and granted the Bureau with supervisory, enforcement, and rulemaking authority over the markets for consumer financial products and services. In addition to creating the CFPB, Dodd-Frank also established the Financial Stability Oversight Council (FSOC) and the Office of Financial Research (OFR) to support it. The FSOC, chaired by the Treasury Secretary, was given the authority to designate certain financial firms as "systemically important" after a review and analysis of the subject company in consultation with functional regulators and the company itself. Systemically important financial institutions and banks with assets greater than $50 billion currently are subject to greater regulatory scrutiny. Dodd-Frank also required banking agencies to establish minimum capital requirements for banking institutions, tightened regulations on debit card interchange fees, eliminated the OTS by folding its functions into other regulatory agencies, and imposed stress tests on financial institutions with $100 billion or more in assets. The stress test is an annual test conducted by the Fed to determine whether the institution being tested is adequately capitalized to withstand adverse economic conditions, using models to forecast outcomes across different scenarios.

The implementation and certain components of Dodd-Frank have been subject to ongoing debates since its inception. This is largely due to the overarching nature (the components mentioned above represent only a synopsis of the regulations that affect banking and payments) and its relative infancy compared to the other laws mentioned in this Basic. Critics of Dodd-Frank have highlighted how excessive regulations, such as bank capital requirements and leverage limitations, have made certain business operations uneconomical or overburdened corporations, driving up costs. Critics contend these negative effects have adversely impacted smaller financial institutions, reduced the supply of credit, and even affected consumers, as financial industries need to charge more for their services. However, proponents conversely argue that Dodd-Frank was simply a reaction to the causes of the Great Financial Recession, and that the new regulations have strengthened the U.S. economy. How this bill is implemented is likely to change in subsequent years, with the potential for amendments to the legislation.

Links to Other Resources

- American Banking Association – Acts & Regulations
- Bank Policy Institute – Bank Regulation 101
- Cornell Law School – Chartering and Field of Membership Manual
- Federal Deposit Insurance Corporation – Chronology of Selected Banking Laws
- Federal Reserve Bank of Chicago – Utilizing the Bank Holding Company
- Federal Reserve History – Bank Holding Company Act of 1956
- Federal Reserve History – Financial Services Modernization Act of 1999 (Gramm-Leach-Bliley)
- Federal Reserve History – National Banking Acts of 1863 and 1864
- Federal Reserve History – Savings and Loan Crisis
- Investopedia – A Primer on Important U.S. Banking Laws
- Investopedia – Thrift Bank: Definition, History, How It Works, and Impact
- National Credit Union Administration – Deposits Are Safe in Federally Insured Credit Unions
- National Credit Union Administration – Historical Timeline
- National Credit Union Administration – Starting a New Federal Credit Union
- Online Lenders Association - Online Lending: Fintech Innovation Drives Credit Inclusion