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ELECTRONIC FUNDS TRANSFER AND
THE SMALL BANK

RICHARD PETERSON*

I. AN INTRODUCTION TO THE INDEPENDENT BANKERS
ASSOCIATION OF AMERICA

The Independent Bankers Association of America (IBAA) is a forty
year old trade group comprised of about fifty percent of the commer-
cial banks in the United States. The IBAA membership includes
locally owned rural and suburban banks and excludes banks or corpora-
tions controlled by multi-bank holding companies. The fundamental
difference between the American Bankers Association (ABA) and
IBAA lies in their attitudes toward competition. The ABA favors
free competition in the banking industry, whereas the IBAA advocates
closer government regulation of industry growth by restricting entry
to firms that prove a business need and convenience. The IBAA claims
that free competition would result in the concentration of deposits in a
few large national banks and holding companies. Because the federal
government, in fact, abets concentration, the IBAA relies on state
governments to balance the federal power and provide the necessary
regulations to prevent concentration, e.g. restrictive branching and
bank holding company laws.

II. THE IBAA'S POSITION ON ELECTRONIC FUNDS
TRANSFER (EFT) DEVELOPMENT

In 1971, the IBAA recognized the technological feasibility of a
national EFT system and began considering its transforming influence on
the banking industry. Because most small banks could not maintain
an expensive EFT system, the IBAA believed that this new technology
would severely impair the ability of these banks to compete with the
large national banks that could provide additional services with EFT.\(^1\)
The IBAA, therefore, refused to be stampeded by the supporters of
national EFT and began a campaign to protect smaller banks in not

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1. See, e.g., AMERICAN BANKERS ASSOCIATION, REMOTE ELECTRONIC FACILITIES,
AN ANALYSIS OF ENABLING ACTS (1976); PEAT, MARWICK, MITCHELL & CO., STATE-
MENT ON THE UNREGULATED DEVELOPMENT OF ETS V-6 (1976) (prepared for IBAA).

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only the Congress, where the National Commission on Electronic Fund Transfers (EFT Commission)\(^2\) was being founded, but also in the state legislatures, the courts, and the administrative agencies.

The IBAA is presently attacking\(^8\) a regulation promulgated by the Federal Home Loan Bank Board (FHLBB) that allows federal savings and loan associations to operate point-of-sale (POS) terminals and automated teller machines (ATMs).\(^4\) Both POS terminals and ATMs perform teller functions at a site remote from the savings and loan office. By installing these terminals in retail stores, customers can deposit or withdraw cash from their savings accounts without appearing at the savings and loan office.

Prior to the IBAA's suit against the FHLBB, the state of Nebraska contested this regulation in *Nebraska ex rel. Meyer v. American Community Stores (Hinky Dinky)*.\(^6\) Hinky Dinky, a food store chain, operated a full-scale teller operation for a federal savings and loan association. Nebraska charged Hinky Dinky with violation of a state statute that prohibits general corporations from engaging in the depository business and argued that the FHLBB could not cure this defect by promulgating regulations applicable only to federal savings and loan associations.\(^6\) The court held, however, that by serving as an intermediary, Hinky Dinky was not a debtor to the savings and loan association's customers and, therefore, was not engaged in the depository business.\(^7\)

The complaint in *Independent Bankers Association of America v. Federal Home Loan Bank Board*,\(^8\) still in the discovery stage, charges that federal savings and loan associations do not have the statutory power to operate POS terminals and ATMs.\(^9\) The Federal Home


\(^5\) Nebraska ex rel. Meyer v. American Community Stores, 193 Neb. 634, 228 N.W.2d 299 (1975).

\(^6\) Id. at 638, 228 N.W.2d at 302.

\(^7\) Id.

\(^8\) No. 76-0105 (D.D.C., filed Jan. 19, 1976).

\(^9\) See text accompanying notes 3 & 4 supra.
Owner's Loan Act of 1933\textsuperscript{10} provides for the establishment of savings and loan associations to offer savers a place to invest at interest rates higher than those of commercial banks and to provide borrowers with a pool of credit to finance housing.\textsuperscript{11} It did not, however, authorize these institutions to provide services to meet their depositors' daily cash requirements. Therefore, courts should note that a leading California savings and loan association has admitted POS and ATM terminals are used for such requirements\textsuperscript{12} and should prohibit the use of POS terminals and ATMs by these institutions. This action will reasonably contain EFT development and confine the federal savings and loan industry to its congressionally defined function.

The IBAA has also resisted federal efforts to encourage EFT development in the banking industry. In \textit{Independent Bankers Association of America v. Smith},\textsuperscript{13} the IBAA maintained that the Comptroller of the Currency could authorize the use of ATMs and POS terminals by nationally chartered banks only on the same terms provided competing state banks under state law.\textsuperscript{14} The Comptroller, on the other hand, argued that these terminals were not branches, but simply conduits of information.\textsuperscript{15} The United States Court of Appeals for the District of Columbia\textsuperscript{16} held that the Comptroller's definition of branch conflicted with the congressional purpose of the National Bank Act of 1933\textsuperscript{17} to promote competitive equality between nationally and state chartered banks. Therefore, the state, rather than the Comptroller, must define "branch."\textsuperscript{18} This decision, in effect, shifted the control of EFT legis-
lation affecting commercial banks from the federal to the state government.

III. OTHER AREAS FOR STATE REGULATION OF EFT

EFT is creating new consumer law problems. For example, suppose an elderly woman received an unrequested bank debit card, her nurse stole the card, and in 10 days withdrew $6,000. The bank could refuse to assume liability because no signatures were involved under the Uniform Commercial Code.19 Similar problems are likely in divorce circumstances. States and the National Conference of Commissioners on Uniform State Laws must confront these consumer problems and develop effective methods of combatting them.

States should also consider the needs of their citizens when enacting mandatory sharing laws providing for the use of EFT terminals by more than one bank. The EFT Commission's report20 relies too heavily on the federal antitrust laws and should not be followed; it would invalidate the laws of many states which approve mandatory sharing.21 IBAA believes that if the state wants mandatory sharing and is willing to shelter such systems from the Sherman Act,22 the federal government should not preclude them from so doing. In *Parker v. Brown*,23 the Supreme Court held that the Sherman Act was not intended "to restrain state action or official action directed by the state."24 This doctrine may validly be applied to state laws controlling EFT and requiring mandatory sharing for the benefit of its citizens.

19. U.C.C. § 1-201(39).
20. NATIONAL COMMISSION ON ELECTRONIC FUND TRANSFERS, supra note 2.
24. Id. at 351.
IV. Future EFT Developments

The IBAA predicts that the EFT Commission's report\(^{25}\) will be ignored. Congressmen supporting legislation which enacts the Commission's recommendation will collide with powerful interests. For example, it is inconceivable that food chains will follow the EFT Commission's recommendation to permit two or three terminals at each checkout counter in the interest of competition. Similarly, food chains want to expand, rather than limit, the number of banks having access to EFT systems. Mandatory sharing achieves that goal. If EFT is to substitute for checks, it must be as flexible as checks. Although flexibility will not necessarily require mandatory sharing, state governments should be free to experiment with methods to control and encourage EFT development. Their judgment should not be overridden by Congress.

In the future, the only way to secure sufficient transaction volume to make EFT feasible for smaller banks will be through the use of large joint systems. If these systems operate in interstate markets, the states can negotiate the reciprocal operation of their laws. Finally, the focus of the debate over EFT development will shift from the branch issue to EFT consumer issues, similar to those addressed in the Uniform Commercial Code,\(^{26}\) and the problem of enacting federal and state technical standards for EFT.\(^{27}\)

\(^{25}\) See National Commission on Electronic Fund Transfers, supra note 2.

\(^{26}\) See, 2 F. Hart & W. Willier, Commercial Paper under the Uniform Commercial Code § 2.05 (1976); McGonigle, Application of Uniform Commercial Code to Software Contracts, 2 Computer L. Serv. 77.

\(^{27}\) The importance of enacting EFT standards in developing workable information systems is demonstrated by the Federal Reserve System's experience with their paper funds transfer system. See Knight, The Changing Payments Mechanism: Electronic Funds Transfer Arrangements, Federal Reserve Bank of Kansas City, Monthly Rev. 10, 18-20 (July-Aug., 1974).