***Financial Markets and Institutions, 7e* (Saunders)**

**Chapter 14 Other Lending Institutions: Savings Institutions, Credit Unions, and Finance Companies**

1) Of all the depository institutions, as a percentage of assets, credit unions rely the most on deposit sources of funds.

Answer: TRUE

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

2) The policy employed in the 1980s of not closing economically insolvent savings institutions was called regulatory forbearance.

Answer: TRUE

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-01 Recognize the differences among a savings institution, a credit union, and a finance company.

Accessibility: Keyboard Navigation

3) After deposits, the second largest source of funds at savings institutions is FHLB loans.

Answer: TRUE

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-02 Identify the main assets and liabilities held by savings institutions.

Accessibility: Keyboard Navigation

4) Savings institutions must have at least 65 percent of their assets in mortgage-related areas in order to maintain their thrift charter.

Answer: TRUE

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-01 Recognize the differences among a savings institution, a credit union, and a finance company.

Accessibility: Keyboard Navigation

5) In a mutual organization, the depositors are owners of the institution.

Answer: TRUE

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-02 Identify the main assets and liabilities held by savings institutions.

Accessibility: Keyboard Navigation

6) Traditionally, most credit union members had a common employer, but increasingly the required commonality is a common location of either residence or workplace.

Answer: TRUE

Difficulty: 1 Easy

Topic: Credit Unions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

7) Savings institution deposits and bank deposits are backed by two different insurance funds.

Answer: FALSE

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-03 Know who regulates savings institutions.

Accessibility: Keyboard Navigation

8) Credit unions are not taxed and, as a result, well-run credit unions are often able to charge lower loan rates and pay slightly higher deposit rates than banks.

Answer: TRUE

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

9) The National Credit Union Administration is the primary regulator of federally chartered credit unions.

Answer: TRUE

Difficulty: 1 Easy

Topic: Credit Unions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

10) There are more credit unions than other types of thrifts, but credit unions are generally smaller than other types of thrifts.

Answer: TRUE

Difficulty: 1 Easy

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

11) The largest U.S. banks are larger than the entire credit union industry.

Answer: TRUE

Difficulty: 1 Easy

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

12) Because of the differences in the makeup of their major loan types, finance companies typically have shorter-term loans than banks.

Answer: TRUE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

13) Sales finance institutions specialize in loan sales to banks and thrifts.

Answer: FALSE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

14) Generally, consumer finance companies make loans to borrowers who have been refused loans at banks due to low income or poor credit.

Answer: TRUE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

15) Generally, a captive finance company is wholly owned by major manufacturing companies with the purpose of providing financing to customers purchasing the parent company's product.

Answer: TRUE

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

16) Factoring is the term used when a finance company purchases accounts receivable from corporate customers at premium.

Answer: FALSE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

17) Floor plan loan is a type of short-term loan to finance high priced inventory in which the purchased inventory is placed as collateral for the loan.

Answer: TRUE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

18) Finance companies are regulated at the federal and state levels similar to commercial banks.

Answer: FALSE

Difficulty: 2 Medium

Topic: Regulation

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Examine the extent to which finance companies are regulated.

Accessibility: Keyboard Navigation

19) Finance companies rely primarily on bank loans and commercial paper as source of funding.

Answer: TRUE

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

20) On average, finance companies have higher capital-to-total-asset ratio than that of commercial.

Answer: TRUE

Difficulty: 2 Medium

Topic: Regulation

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Examine the extent to which finance companies are regulated.

Accessibility: Keyboard Navigation

21) Which of the following trends in the number and industry assets of savings institutions is/are correct?

I. The number of savings institutions has fallen over time.

II. The number of savings institutions has increased over time.

III. Total industry assets fell during the recession of the late 2000s.

IV. Total industry assets are falling over time.

V. Total industry assets are stable but the number of savings institutions has fallen.

A) II and III only

B) I and III only

C) I and IV only

D) II and IV only

E) V only

Answer: B

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Understand; Remember

AACSB: Reflective Thinking

Learning Goal: 14-04 Discuss how savings institutions performed in the 2000s.

Accessibility: Keyboard Navigation

22) The QTL test requires that thrifts

A) limit the amount of mortgage-related assets on the balance sheet to improve diversification.

B) invest in a minimum percentage of government-backed securities to protect their mortgage loans.

C) lend no more than 80 percent of the value of a home to a borrower to ensure mortgage safety.

D) keep 35 percent of their assets in safe liquid investments to ensure adequate deposit liquidity.

E) invest at least 65 percent of their assets in mortgages or mortgage-related assets.

Answer: E

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-01 Recognize the differences among a savings institution, a credit union, and a finance company.; 14-02 Identify the main assets and liabilities held by savings institutions.

Accessibility: Keyboard Navigation

23) Which one of the following has the highest concentration of mortgage-related assets on the balance sheet?

A) Savings institutions

B) Commercial banks

C) Credit unions

D) Finance companies

E) Pension funds

Answer: A

Difficulty: 1 Easy

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-02 Identify the main assets and liabilities held by savings institutions.; 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

24) After 2011, savings institutions have primarily been regulated by

A) Federal Home Loan Bank Board.

B) Federal Deposit Insurance Corporation.

C) Office of Thrift Supervision.

D) National Credit Union Administration.

E) Office of the Comptroller of the Currency.

Answer: E

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-03 Know who regulates savings institutions.

Accessibility: Keyboard Navigation

25) In 2016, the largest U.S. savings institution was

A) USAA Federal Savings Bank.

B) Synchrony Bank.

C) Navy Federal.

D) Hudson City Bancorp.

E) Charles Schwab Bank.

Answer: E

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-04 Discuss how savings institutions performed in the 2000s.

Accessibility: Keyboard Navigation

26) The predominant liabilities for savings institutions are

A) commercial deposits and FHLB borrowings.

B) wholesale money market notes and reserves at the Fed.

C) transaction accounts, small time and savings deposits.

D) checking accounts and money market mutual funds.

Answer: C

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-02 Identify the main assets and liabilities held by savings institutions.

Accessibility: Keyboard Navigation

27) Historically, most savings institutions were established as

A) mutual organizations.

B) stockholder organizations.

C) partnerships.

D) charitable organizations.

E) banks.

Answer: A

Difficulty: 1 Easy

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-02 Identify the main assets and liabilities held by savings institutions.

Accessibility: Keyboard Navigation

28) Deposits at savings banks are backed by the \_\_\_\_\_\_\_\_ and deposits at savings institutions are backed by the \_\_\_\_\_\_\_\_.

A) BIF; BIF

B) BIF; SAIF

C) SAIF; BIF

D) SAIF; SAIF

E) DIF; DIF

Answer: E

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-03 Know who regulates savings institutions.

Accessibility: Keyboard Navigation

29) \_\_\_\_\_\_\_\_ are the most diversified of depository institutions and \_\_\_\_\_\_\_\_ are on average the largest depository institutions.

A) Banks; savings institutions

B) Credit unions; commercial banks

C) Credit unions; credit unions

D) Commercial banks; commercial banks

E) Savings institutions; commercial banks

Answer: D

Difficulty: 2 Medium

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-02 Identify the main assets and liabilities held by savings institutions.; 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

30) Credit unions are

I. mutual associations.

II. not open to the general public.

III. for profit institutions.

A) I only

B) II only

C) I and II only

D) I, II, and III

E) II and III only

Answer: C

Difficulty: 1 Easy

Topic: Credit Unions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

31) The U.S. Central Credit Union and the corporate credit union

A) are the primary regulators of the credit union industry.

B) provide investment and liquidity services to corporate credit unions.

C) serve as the trade organization for the industry.

D) charter credit unions.

E) provide deposit insurance for credit unions.

Answer: B

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

32) Credit unions have several advantages over banks. These include the following:

I. Credit unions are not taxed.

II. Credit unions are better diversified than banks.

III. Credit unions can collectively pool funds.

IV. Due to regulations, credit unions have better economies of scale and scope than banks.

V. Because of their ties to employers, credit unions have better personnel expertise than banks.

A) I and II only

B) I and III only

C) III and IV only

D) III, IV, and V only

E) I, III, and V only

Answer: B

Difficulty: 3 Hard

Topic: Credit Unions

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

33) As a percentage of total assets, credit unions invest \_\_\_\_\_\_\_\_ in securities than savings institutions and \_\_\_\_\_\_\_\_ in consumer loans than commercial banks.

A) more; more

B) less; less

C) more; less

D) less; more

E) less; about the same

Answer: A

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

34) SI profitability declined in the mid-2000s due to

I. the yield curve becoming more positively sloped.

II. decreases in the NIM ratio.

III. increases in the NIM ratio.

IV. the yield curve becoming flatter and even inverted.

A) I and II only

B) II and III only

C) II and IV only

D) III and IV only

E) I and III only

Answer: C

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Understand

AACSB: Reflective Thinking; Analytical Thinking

Learning Goal: 14-04 Discuss how savings institutions performed in the 2000s.

Accessibility: Keyboard Navigation

35) Rank the following from greatest to smallest in terms of industry asset size in 2016.

I. Banks

II. Savings institutions

III. Credit unions

IV. Finance companies

A) IV, I, II, III

B) I, IV, III, II

C) I, II, IV, III

D) I, II, III, IV

E) II, IV, III, I

Answer: B

Difficulty: 3 Hard

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-02 Identify the main assets and liabilities held by savings institutions.; 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

36) In 2016, \_\_\_\_\_\_\_\_ had on average the greatest amount of equity as a percentage of assets and \_\_\_\_\_\_\_\_ had the lowest.

A) savings institutions; credit unions

B) banks; credit unions

C) credit unions; finance companies

D) finance companies; credit unions

E) finance companies; banks

Answer: D

Difficulty: 3 Hard

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-02 Identify the main assets and liabilities held by savings institutions.; 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

37) Factoring is

A) equipment leasing.

B) servicing mortgage factors.

C) purchasing corporate accounts receivables at a discount.

D) financing automobile purchases.

E) making installment loans to customers.

Answer: C

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

38) Sales finance companies

A) specialize in making loans to customers of a specific retailer or manufacturer.

B) specialize in making installments and other loans to whatever consumers are interested.

C) specialize in providing loans to businesses.

D) specialize in international factoring and forfeiting.

E) None of these options are correct.

Answer: A

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

39) A finance company that makes loans to high-risk customers is called a

A) subprime lender.

B) commercial bank.

C) factor.

D) warehouse lender.

E) credit lender.

Answer: A

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

40) Finance companies enjoy several advantages over banks. These include all but which one of the following?

A) Finance companies can offer various types of products and services without regulatory interference.

B) Many finance companies have considerable knowledge and expertise about specific industries and products.

C) Finance companies can accept riskier customers than banks.

D) Finance companies generally have lower overhead than banks.

E) Finance companies have lower funds costs than banks.

Answer: E

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

41) A captive finance company is one that

A) is owned by a retailer or manufacturer.

B) is owned by a bank holding company.

C) is owned by its depositors.

D) lends only to high-risk individuals that cannot obtain loans elsewhere (i.e., captives).

E) is regulated at the federal level.

Answer: A

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

42) A loan agreement between Ford Motor Credit and a local Ford dealer is an example of

A) floor plan financing.

B) business equipment loan.

C) factoring of receivables.

D) depreciation loan.

E) None of these options are correct.

Answer: A

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

43) Home equity loans are popular with finance companies. Which one of the following statements about home equity loans is not correct?

A) These loans allow customers to borrow on a line of credit secured with a second mortgage.

B) Interest payments on home equity loans are not tax deductible.

C) Bad debt expenses on home equity loans are lower than on many other types of finance company loans.

D) In 2007–2008 there was a sharp increase in defaults among home equity borrowers.

E) If the borrower defaults on the home equity loan, the finance company can seize the house.

Answer: B

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

44) For the finance company industry as a whole, the largest single loan type is

A) business loans.

B) consumer loans.

C) real estate loans.

D) high-risk consumer loans.

E) credit card loans.

Answer: B

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

45) Aggregate finance company profitability was poor in the late 2000s primarily due to which segment of the finance company industry?

A) Business factoring

B) Equipment loans

C) Equipment leasing

D) Securitization of auto loans

E) Subprime lending

Answer: E

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

46) Which one of the following utilizes the least amount of deposits as a source of funds?

A) Banks

B) Credit unions

C) Finance companies

D) Savings associations

E) Savings banks

Answer: C

Difficulty: 1 Easy

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-02 Identify the main assets and liabilities held by savings institutions.; 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

47) Finance companies obtain a significant portion of their short-term financing from

A) time and savings deposits.

B) transaction accounts.

C) long-term bonds.

D) issuing commercial paper.

E) equity.

Answer: D

Difficulty: 1 Easy

Topic: Finance Companies

Bloom's: Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

48) Which one of the following institutions is the least regulated?

A) Banks

B) Credit unions

C) Finance companies

D) Savings associations

E) Savings banks

Answer: C

Difficulty: 1 Easy

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.; 14-03 Know who regulates savings institutions.; 14-09 Examine the extent to which finance companies are regulated.

Accessibility: Keyboard Navigation

49) In 2016, credit union's biggest type of loans was \_\_\_\_\_\_\_\_.

A) mortgages

B) business loans

C) consumer loans

D) home equity loans

E) government loans

Answer: C

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

50) In 2016, credit union's largest portion of investment securities was \_\_\_\_\_\_\_\_.

A) treasury debt

B) corporate bonds

C) federal agency securities

D) mortgage-backed securities

E) asset-backed securities

Answer: C

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

51) Explain why low interest rates and strong mortgage markets help keep profitability high at savings institutions.

Answer: Low interest rates have helped savings institutions (SIs) maintain profitability because many thrifts fund long-term mortgages with short-term deposits. Low interest rates have encouraged mortgage refinancing and new home buying; both activities allow thrifts to earn origination and servicing fees and to profit on the spread between interest earned on the mortgages and costs paid on deposits. Because SIs concentrate in mortgages, the health of the housing industry will strongly affect their profitability. Because many mortgages are sold, the default risk may not lie with the originating SI, but defaults will result in tighter origination standards and less fees for the originating institution. Higher default rates will affect the mortgage portfolio that SIs keep and can result in impaired capital and poor profitability.

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-04 Discuss how savings institutions performed in the 2000s.

Accessibility: Keyboard Navigation

52) A savings institution (SI) has funded $12 million of 30-year fixed-rate mortgages with an average interest rate of 5.75 percent. These assets are funded with time deposits with an average maturity of six months. The deposits are currently paying 3.5 percent. In six months time, however, the Fed has raised interest rates twice and the depositors now must be paid 4.25 percent. What will happen to the SI's ROA and NIM? How would your answer change if the SI normally sells the mortgages every six months and originates additional new mortgage loans?

Answer: The original gross profit margin was 5.75% − 3.5% = 2.25%, and after six months the profit margin on these loans falls to 5.75% − 4.25% = 1.50%. This will reduce the SI's ROA and NIM, ceteris paribus. If the SI is selling the mortgages every six months, however, the new mortgage rates may be sufficiently higher to offset the rising deposit interest rates, thus preserving the profit margin and ROA and ROE.

Difficulty: 2 Medium

Topic: Savings Institutions

Bloom's: Analyze; Apply; Evaluate

AACSB: Reflective Thinking; Analytical Thinking

Learning Goal: 14-04 Discuss how savings institutions performed in the 2000s.

Accessibility: Keyboard Navigation

53) What are the major advantages that credit unions enjoy over banks?

Answer: Advantages of credit unions are as follows:

* Credit unions are not taxed because of their nonprofit status. The CU should be able to offer either lower loan rates or pay higher deposit rates because of the tax advantage.
* Credit unions are allowed to pool funds with each other and invest their funds collectively in money and capital markets through the corporate central and U.S. central credit unions. Credit unions may obtain loans from these entities and receive management advice.

*The following three are not in the text:*

* Employer-based credit unions may require loan payments to be directly deposited to the credit union, reducing processing and collection costs.
* Credit unions often receive donated services and donated facilities that help keep their costs down.
* Credit union regulators are not as adversarial as bank regulators. They act to promote as well as regulate the industry.

Difficulty: 3 Hard

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

54) What are the major disadvantages that credit unions face versus banks?

Answer: Disadvantages of credit unions are as follows:

* Credit unions are under-diversified due to the common bond requirement. An employer-based credit union could experience simultaneous loan defaults and deposit withdrawals due to employer default layoffs or strikes.
* Credit unions are much smaller than the average bank. Credit unions may have to operate well below the size that would generate optimal economies of scale and scope.
* Credit unions lack the skills necessary to offer other financial services such as insurance, brokerage, and so forth.
* Credit unions lack expertise to evaluate business loans and cannot offer many of the services larger banks can.
* *Not in text:* Credit unions have difficulty attracting quality personnel to serve as managers. Often, the board of directors and/or senior personnel serve on a voluntary basis.

Difficulty: 3 Hard

Topic: Credit Unions

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

55) How do the primary risks of credit unions differ from banks? from savings institutions (SIs)? from finance companies?

Answer: Credit unions face credit risk on consumer loans, but banks have credit risk on consumer and business loans and many off-balance-sheet activities. Business loan evaluation is more complex, and banks are generally involved in riskier loans than either credit unions or SIs (with the possible exception of SI involvement in commercial real estate). The lack of diversification of a credit union also adds to its risk. Bank deposits, particularly large deposits and business accounts, are likely to be more sensitive to interest rates than credit union deposits.

Credit union customers exhibit more loyalty than typical bank and SI customers. Credit unions hold more liquid assets (%) than banks or SIs, and they can afford to do so because of the lack of a profit motive. SI loans are usually well collateralized but longer term than their liabilities, generating interest rate risk. Credit unions do not normally have a large imbalance between the maturity of their assets and liabilities. Credit unions face regulatory risk because of the recent lawsuits by banks attempting to limit the growth of credit unions.

Some finance companies lend to higher-risk consumers; some are much more extensively involved in business loans than credit unions. Finance companies are larger so they may provide services more cost-effectively than the small credit unions. Finally, finance companies cannot take deposits so they are denied the steady, low-cost source of funds that credit unions enjoy.

Difficulty: 3 Hard

Topic: Credit Unions; Savings Institutions; Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

56) The American Bankers Association and others are seeking to limit growth of credit unions. What is the basis for the bankers' concern? What does the credit union industry argue? What kind of limits on credit unions are the bankers seeking?

Answer: The bankers are arguing that credit unions can unfairly compete with banks for consumer loans and deposits because credit unions are not taxed. The tax advantage allows credit unions to offer higher rates on deposits and lower rates on loans in most cases. The common bond requirement is designed to limit competition among credit unions (each other) and between banks and credit unions. Historically, credit union members were sponsored primarily by an employer, and most people could not participate in a credit union. The weakening of the common bond requirement and the growth of credit unions have brought this industry into more direct competition with banks for consumer banking services. Banks are seeking to limit growth of credit unions by limiting credit unions' ability to accept new members and to limit the number of community-based credit unions. Community-based credit unions represent the greatest threat to banks because their "common bond" is very broad, namely to live and/or work in a given community.

Difficulty: 3 Hard

Topic: Credit Unions

Bloom's: Understand; Remember

AACSB: Reflective Thinking

Learning Goal: 14-05 Describe how credit unions are different from other depository institutions.

Accessibility: Keyboard Navigation

57) Why have larger credit unions experienced greater profitability than smaller credit unions? Do you expect this to continue? Why or why not?

Answer: Larger credit unions have been more profitable because they have a larger customer base over which they can spread their fixed costs and they tend to be better diversified and thus are more able to weather tougher economic times. Larger credit unions are likely to continue to be more profitable due to economies of scale and scope and the advent of technology (a major fixed-cost investment) in the financial services industry.

Difficulty: 2 Medium

Topic: Credit Unions

Bloom's: Remember; Evaluate

AACSB: Reflective Thinking

Learning Goal: 14-06 Identify the main assets and liabilities held by credit unions.

Accessibility: Keyboard Navigation

58) What are home equity loans? Why do finance companies prefer home equity loans to unsecured debt?

Answer: Home equity loans are loans that pledge the equity value of the home as collateral Finance companies prefer home equity loans to unsecured credit because the collateral reduces the need for an extensive credit check and provides the lender with better collateral in the event of default.

Difficulty: 3 Hard

Topic: Finance Companies

Bloom's: Understand; Remember

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

59) What are the advantages of a finance company or a bank leasing equipment to a small business customer rather than financing the customer's purchase of the equipment?

Answer:

* It is easier for the bank or finance company to repossess the equipment in the event of default with a lease because it retains title to it.
* Lease agreements are easier to sell to companies because many do not have required down payments.
* By retaining ownership, the bank or finance company gets a tax deduction for depreciation of the equipment leased. In some cases the small business will not be able to use the full amount of the depreciation tax shield due to insufficient income, whereas the bank or finance company can.

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

60) How do sales finance companies differ from personal credit and business credit institutions? List an example of each.

Answer: Sales finance companies, such as Ally Financial (formerly GMAC) or Ford Motor Credit, specialize in making loans to customers of a specific retailer or manufacturer; personal credit institutions specialize in loans to consumers, usually to riskier customers. An example of the latter is HSBC Finance. Business credit institutions such as Heller Financial provide financing to corporations via leasing and factoring.

Difficulty: 2 Medium

Topic: Finance Companies

Bloom's: Understand; Remember

AACSB: Reflective Thinking

Learning Goal: 14-07 Define the major types of finance companies.

Accessibility: Keyboard Navigation

61) What are the advantages finance companies (FCs) have over banks in the area of business lending? What disadvantages do they have?

Answer: Finance company advantages include the following:

* Banks have extensive product regulations and FCs do not.
* In many cases FCs have extensive information about company products and the industry because of their ties to manufacturers.
* FCs can lend to riskier customers than banks and, if they are good at credit analysis, can earn a higher rate of return on these customers.
* FCs have lower overhead than banks, because they do not seek retail sources of funds that require substantial investments in brick and mortar (branches).

Bank advantages include the following:

* Many banks are larger and have more expertise in providing a wider range of financial services. These two factors imply that banks can exploit economies of scale and scope and may have higher profitability than finance companies (FCs).
* Banks obtain a major portion of their funds (deposits) at a subsidized cost because of federal deposit insurance. This lowers their funds cost and allows them to carry less equity on the balance sheet, potentially improving the shareholders return on equity.
* Consumer finance companies have the reputation for providing high-risk loans and tend to attract those types of customers. Subprime and consumer FCs are sensitive to the economy because their customers' finances are often hurt by economic downturns, as occurred in late 2007 and 2008.

Difficulty: 3 Hard

Topic: Finance Companies

Bloom's: Understand

AACSB: Reflective Thinking

Learning Goal: 14-08 Identify the major assets and liabilities held by finance companies.

Accessibility: Keyboard Navigation

62) Has the importance of foreign nonbank financial lending been increasing or decreasing in recent years? Provide some examples to back up your answer.

Answer: Nonbank financial lending has gained as a percentage of total lending in many foreign countries including low-income mortgage lending in Mexico, credit card lending in Thailand, and leasing and factoring in Eastern Europe. In Latin America from 1994 to 2010, the percent of aggregate financing provided by nonbank FIs grew from 22 percent to 35 percent. The corresponding numbers for growth in Central Europe are from 4 percent to 15 percent.

Difficulty: 3 Hard

Topic: Global Issues

Bloom's: Understand; Remember

AACSB: Reflective Thinking

Learning Goal: 14-01 Recognize the differences among a savings institution, a credit union, and a finance company.

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