REMARKS BY THE HONORABLE STEPHEN S. GARDNER
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Good Afternoon:

It is a pleasure for me to be here today on the occasion of the opening of your 1976 Governmental Affairs Conference. As your President stated in his introduction, I have been deeply involved in the Administration's Financial Institutions Act, and as part of that effort had to become increasingly aware of the important role credit unions play in our complex financial system.

In reviewing the impressive program for your Conference, I note that during the next several days you will be considering various aspects of the changing financial environment in this country. This is a most appropriate subject, for there is indeed a climate of change here in Washington, one which has given rise to a number of dramatic Congressional initiatives of particular interest to you as members of the financial community.

Before touching specifically on some of these Congressional actions, I would like to share with you a few thoughts concerning the growing clamor for change not only within our financial institutions but also within our society at large.

You have seen the polls allegedly establishing the low regard in which the country holds the Government, the Administration, the Congress and business. Six years ago, 58 percent of the people polled by the Lou Harris organization expressed confidence in major companies. Last year, that figure dropped to 29 percent -- and in the 18-20 year old category only fifteen percent (or 1 in 7) expressed any confidence in the way business is run. Maybe you know the figures for financial institutions. I'm not sure I want to.

This is more than the legacy of hostility and suspicion and despair that the events of Watergate and the more recent incidents of improper corporate behavior have engendered. It is the result of massive and continuing social change brought on literally by our success in this country in terms of economic gains, the freedom of speech and action inherent in a democracy, and the social sensitivities of a great nation.

I think it has gone too far in fragmenting our people and polarizing dissent, but that's the way change operates -- cyclically. In this new world, the marvelous electronic telecommunication system assures that trends develop faster and recede more quickly, and that they are global in nature. And castigating the media is an exercise of futility. The media is popular and it sells. In a free society people get the kind of media they support.

Let's get to the basic problems. Behind the lack of confidence in government and business and our institutions is the presumption that government can make all things right in a private economy -- a presumption ingrained for three decades in America's conscience and a contradictory idea at best. But one that can't be judged objectively in the socio-political-economic climate of today.

After thirty years of generally good growth, increasing wealth, modest inflation, and reasonable level of employment, we have gone through change that stuns us -- change that will have to upset our routine and fairly perceived social goals. And the bulk of our citizens are poorly prepared to deal with the issues. In fact, the issues outweigh our experience of the post-war years -- and all of them haven't even surfaced yet.

First and foremost, if you wish to retain a social system you must maintain a generally acceptable economic system, and that is going to be difficult to do in the short run in the United States. The stated reasons are the persistent threats of inflation and energy shortages. The actual reason is that during the bountiful years when our private sector roared ahead, suffering all the restraints and regulations that we imposed on it, we established by edict, law, and common consent, some very worthwhile and unassailable national goals which are still in the full swing of implementation.

These goals are easy to identify generally -- an expanded Social Security program and benefits to the underprivileged and veterans, a more liberal view of unemployment assistance, medical support for the elderly and indigent, proper housing for all our people, better and more education for all, protection of the environment. The list is very long and you know it well.

I take issue with none of these goals, and I assume you do not either. But a few simple statistics will show you how successful we have been in increasing these transfer payments in our society.

For Fiscal Year 1977 existing laws have mandated Government payments for individuals estimated at $170 billion -- a sum larger than the entire Federal budget outlay of only eight years ago. In 1967, these same programs totalled $41.8 billion. In fact, approximately 75 percent of the Federal budget estimate recently submitted by the President consisted of relatively uncontrollable outlays, and two-thirds of this amount represented transfer payments for individuals. Whatever the virtue of the programs, we are clearly succeeding in funding these national goals.

Now when we began the exercise to assist in stimulating the country in a sharp and dangerous recession last year, we began it with hardly any maneuverability in terms of Government outlays. For all practical purposes, the idea that the Government can stimulate the private economy in periods of recession and control and reduce its expenditures below receipts in periods of prosperity has no basis in the fact or experience in the last half of the thirty years since World War II.

Today, our National goals must also include stimulating employment in the private sector, increasing capital formation to meet the extraordinary capital requirements of the next decade, and managing a quantum jump in energy costs -- the greatest challenge our economy has faced.

How does one begin this process? Thoughtful people have quietly said that we must reorder our priorities and, indeed, there is no alternative. But I suggest it will be a terribly painful and difficult process for this society, which has been led by its hopes and experience to expect the Government to continue to fund its social goals. And the constituents of each and every program have the leverage with the Congress (and, for that matter, with the Administration) to make the process of adjusting priorities a social Vietnam.

Examples are easy to come by. Official studies and reports about the Social Security System indicate a major imbalance in receipts and expenditures under certain rather routine demographic assumptions for the future. This is exhausting the balances in the trust funds (normally one year's retirement benefits) and in a few years will force the use of general revenues. Avoiding that trap could also mean 15 to 20 percent Social Security wage deduction, possibly a worse answer. We must have some objective support for a conscientious, factual overview of the System to correct its deficiencies and balance its costs.

Similarly and more specifically, there must be a massive overhaul of the welfare system, a collection of federal and state programs which are so inefficient and so extensively abused that they beg analysis. In this connection, you know what happened in the President's recent proposals to reform our food stamp practices. A substantial effort must be made to control the mindless escalation to recipients who neither deserve nor were intended to receive the stamps.

In another area, we have all been talking querulously about the massive Federal deficits and what they will eventually do to the capital market. Our capital formation process is already too small for the demands placed upon it -- smaller than any of the other industrialized nations by relative measure in the free world. Gains in productivity are also grinding to a halt in the United States. There has never been a time when we more desperately needed to reverse these trends. But I suggest that reversal has to begin with a new understanding and objectivity about our economy; and if we can get such a discussion moving in a democratic society, it will affect all of the micro-issues which concern our economic world.

It is within this context that we should examine the changes likely to occur in our private financial intermediaries, for traditionally these institutions have reacted to and been significantly affected by social and economic change. The kind of change I think most likely to occur in the short run is suggested by the Financial Institutions Act of 1975, which this past December passed the Senate by a vote of 79-14. The issues presented by the FIA have also been the subject of extensive hearings and discussion before the House Banking, Currency and Housing Committee in its study entitled <u>Financial Institutions and the Nation's Economy</u>.

A principal and important thrust of FIA is to enlarge competition. Our unique system of private financial institutions has tended to be heavily specialized and, in fact, the Government through legislation and regulation has been a party to that process. But our economy is changing, our society has grown more affluent, people's financial needs are indeed more diverse than they were in earlier, simpler days. If more and dramatic evidence is needed for my arguments, I can refer you to the painful disintermediation of the recent past, the net outflows of funds from savings balances, and the havoc that inflation has visited on the small saver.

The FIA is designed to increase the strength of a number of financial institutions by permitting and equipping them to respond more readily to these instances of economic, financial and institutional change. A clear beneficiary of this change will be the consumer. The bill encourages greater competition and provides new opportunities for savers to receive a competitive rate on their investment while providing homeowners with greater assurance that the flow of funds for home mortgages will not be disrupted during periods of high interest rates. If Congress enacts FIA into law, our financial institutions will benefit from the ability to offer new services and enter new markets; and their customers, both depositors and borrowers, will share these benefits.

Under the provisions of the FIA, savings and loans and mutual savings banks will be permitted to offer checking accounts and negotiable order of withdrawal accounts to individuals and businesses, while diversifying a portion of their investments into consumer loans, unsecured construction loans, commercial paper and certain high-grade private debt securities. Commercial banks will be permitted to offer savings accounts and NOW accounts. To improve the availability of mortgage credit, commercial banks, savings and loan associations, mutual savings banks and other taxable financial institutions will be granted a tax credit incentive to enlarge their volume of mortgage loans. The tax credit is presently based on an accelerating formula in the Act, moving from 1.5 to 3.83 percent, depending upon the proportion of assets held in residential mortgages.

In a further effort to aid all banking institutions in the financing of the housing industry, the FIA envisions the elimination of Regulation Q 5-1/2 years after the effective date of the Act. Prior to this date, Regulation Q authority is to be exercised by the regulators in a manner "which prevents disintermediation and maintains appropriate levels of mortgage credit."

Significantly, the FIA provides for a substantial expansion of the asset and liability powers of credit unions. Among these are the granting of checking account powers, the establishment of a central discount fund to obtain funds for short-term liquidity purposes by issuing obligations in the capital market, and the power to make a wider range of loans, including mortgage loans, at more varied interest rates. Credit unions are also granted expanded investment authority with regard to Federal, state and local obligations and are permitted to sell, purchase or handle any money transfer instrument for benefit of their members.

It should be apparent that I believe the FIA to be important legislation which provides a clear statement of national policy on financial reform. It represents a plan for the implementation of balanced reform over the next several years, is comprehensive and I think fair, and should assure the opportunity for sound growth of all affected financial institutions in our changing society. Clearly, the FIA grants to credit unions a number of powers necessary to better serve the interests of your ever-growing constituency.

The FINE Study discussion principles currently under consideration by the House Banking, Currency and Housing Committee incorporate with a few minor variations the provisions of the FIA. But the FINE Study goes well beyond FIA-type reforms in its proposals to support housing, consolidate the regulatory agencies, restructure the Federal Reserve System, and establish new regulation of foreign banking in the United States and U.S. banks operating abroad. Representative Henry Reuss, Chairman of the House Banking, Currency and Housing Committee, hopes to begin hearings in two weeks on these sweeping proposals, and has publicly announced his intention to see financial reform enacted into law before the first of July. I sense that Mr. Reuss' timetable is realistic, and although I personally do not believe we will have radical change within the banking industry this year, I believe we will indeed have change--perhaps even aggressive change.

With these changes will come new challenges for all financial institutions, including credit unions. But if past performance is any barometer of future accomplishment, and I think it is, then credit unions surely possess the dedication and ability to meet these new challenges.

The last decade has materially changed the financial environment in which credit unions must function. Growing inflation, resulting in part from the Vietnamese war and in part from oil, raw material and agricultural shortages, has been responsible for a series of basic increases in the levels of interest rates, aggravated by attempts to halt the rise in prices. Certificates of deposit, liquid asset mutual funds and an increased volume of capital market instruments resulting from the heavier financing activity of Federally-sponsored agencies have appeared as major new alternatives for the saver. Charge cards and the growth of credit extensions by such nonfinancial retail firms as Sears Roebuck and J.C. Penney have greatly increased the degree of competition in consumer finance. Service corporations, holding companies and other innovations in institutional structure have opened up new competition in the financial industry. The growth of Federally sponsored credit agencies and such housing-related private institutions as FNMA, have materially changed the markets for mortgage credit. On the whole there has probably been a greater change in our financial institutions during the past ten years than during any comparable period since the mid-nineteen thirties.

And there is little evidence to suggest that this trend will abate in the coming post-Bicentennial decade. The modifications to the powers and responsibilities of our financial institutions as proposed in the FIA and the FINE Study will bring with them concomitant changes in the operating practices of the affected institutions. Recent hearings on a Federal Reserve Board proposal to regulate the operations of foreign banks in the United States, on a Senate bill to consolidate the examination and supervisory agencies -- the FDIC, Fed and Comptroller -- into a single agency, and on a proposal which would limit acquisitions or mergers of certain banking institutions, suggest that we might well see substantive changes in these areas in the near future.

There are many other significant challenges which will confront our financial institutions in the next few years. The development of a widespread electronic funds transfer system, and the corresponding revolution in our payments systems is on the near horizon. The National Commission on Electronic Funds Transfers, on which you are most ably represented by Herb Wegner, has within the past few weeks begun to focus carefully on the multitude of new and complex financial and social questions presented by the use of such a system. We must within the very near future find a way to finance the research and development necessary to relieve our growing energy shortages. We must develop new and effective approaches to meet the recurring problem of housing finance, the critical challenge of increased capital formation, and the ever-growing needs and demands of customers of all our financial institutions. And these are only a few of the many positive steps we must take.

As you move through your discussions at this meeting to consider the changing financial environment, and the challenges ahead, I hope you will consider broadening your involvement to include the wider economic challenges to our society. I don't mean expressing your views to the many Administration officials to whom you have access. Nor do I particularly mean only to the Congress. I refer to the broad public that credit unions service, to all of your customers, large and small, in the multitude of communities throughout this nation where you carry on your operations. You can do a great deal by codifying the economic risks we face, and by explaining the technicalities that so often mystify the general public.

There is no doubt we will have many challenges in the decade ahead, both in our financial intermediaries and on a broader scale in our institutions at large. As leaders in your industry and leaders in your communities you can provide a great service by assisting your nation's policymakers in the formulation of effective and lasting solutions to these challenges.

And I think you should do that. Because while we are all interested inevitably in our own industry -- and the FIA and FINE legislation provide many new advantages to credit unions -- none of our financial intermediaries will prosper if our private economy is diminished. I suggest that the Bicentennial year could be more important in our history than an anniversary. It may well be the year we determine as a nation to return to sound and moderate fiscal goals and as I look at the extraordinary past achievements of this nation I think that would be something to celebrate.

Thank you