For release 3:30 p.m.
Eastern Standard Time
February 19, 1971

Remarks of J. L. Robertson

Vice Chairman of the Board of Governors
of the
Federal Reserve System

before the

University of Miami
Savings Institutions Forum

Doral Hotel and Country Club

Miami, Florida

February 19, 1971

An Idea and Its Hour

Thanks to my recent book, "What Generation Gap???", I have become associated in the minds of some people with the widespread concern about the unconventional aspirations of our young people. The youth frequently tend to be quite critical of the imperfections in our society. But this is not limited to the younger generation. Most of us believe that we can make things better, and we work hard to do so, but we realize that we cannot really expect to attain perfection. Of course, there are always a few who want perfection and will settle for nothing less.

One such person came charging into Charlie Black's shoe store back in my home town, Broken Bow, Nebraska. She shoved a pair of snakeskin shoes under Charlie's nose and said, "I just bought these shoes here yesterday. When I took them home I noticed that they had little scratches all over them." Charlie looked at the shoes, and sure enough the tiny marks were there. He went back and got another pair, but when the lady looked at them she discovered that they, too, had little marks on them. Charlie patiently took out another pair, and still another, but they were no different. Finally, he threw up his hands and said, "Well, lady. I'm not perfect, and you're not perfect. How in heaven's name can we expect a snake to be perfect?"

While most of us do not expect perfection, one of the characteristics of a vital, dynamic people is their interest in improving themselves, their institutions, and their environment. As I look over our entire system of financial institutions and the regulatory superstructure that has developed over the years, I can see a great deal of room for improvement.

Consequently, I want to take my text today from a sentence in Victor Hugo's "Story of a Crime", which has been variously translated but whose most felicitous English rendition is perhaps "Greater than the tread of mighty armies is an idea whose hour has come." I would like to use this text to focus on some recent happenings, seemingly disconnected, but which in fact may constitute a cluster of essentially interdependent consequences, produced by the same underlying causes, addressed ultimately to the same solution, and marking the hour of arrival of an idea which I have advocated in one form or another for many years. The current thrust of that idea may be summed up in two distinct but related propositions.

First, that all mutual savings banks and savings and loan associations be allowed - at their own choice - to evolve into broad-gauged lenders and borrowers along the lines of commercial banks via an appropriate transitional process which will eventually subject them to the full array of reserve requirements, tax liabilities, supervisory limitations, and other responsibilities of banking institutions.

Second, that the supervisory and chartering responsibility now fragmented among the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the Federal Reserve be unified in one independent agency administering a common set of ground rules for all bank-type institutions under federal supervision.

I have pleaded the case for this idea for some time. Since 1962 I have advocated placing all federal banking supervision in a single agency. Since 1966 I have proposed parity for bank-type institutions subject to federal law. Why does the hour of this idea seem to have come - or be fast approaching - in 1971? For two reasons, I think: First, it is because the trillion-dollar economy has now arrived, and, paradoxically, one thing that the trillion-dollar economy simply cannot afford in terms of the vital financial resource of our depositary institutions is the doctrine of separate and unequal. Second, there is growing apprehension, perhaps below the level of full consciousness and possibly addressed to parts of the problem rather than the whole, that there are matters which public policy has already declared to be of highest priority - indeed of highest urgency - but where the declaration of purpose has been increasingly impeded and checkmated by elements of mechanism and technique. These two circumstances have combined to set in motion a strong tide which is already sweeping toward its logical conclusion - a leveling of existing disparities and a resultant restructuring of both financial infrastructure and its supervisory overlay.

As evidence of this tide, I invite your attention to the following seemingly unconnected but actually very closely linked developments of the recent past:

First - the unprecedented resort of S & L's to money raised through the securities market via the Federal Home Loan Banks. During the credit pinch of 1969, for example, S & Ls' source of investment capital broadened to the point where more funds were raised indirectly through the securities market by borrowing from the Home Loan Banks than were obtained directly from savers.

Second - the announcement by the Chairman of the House Banking and Currency Committee late last year that he would offer a bill in the 92nd Congress granting Savings and Loans authority to offer complete checking account services, accept deposits of Treasury tax funds, have full access to the Federal Reserve Banks' discount window, and make more consumer loans, particularly for household items.

Third - the record number (though still small) of mergers or conversions of S & L's into savings banks during 1970.

Fourth - the regulations issued by the Home Loan Bank Board in 1970 governing third party payments by federal savings and loan associations; and

Fifth - the enactment last year of the so-called One-Bank Holding Company Act, sweeping under Federal Reserve jurisdiction some 1,100 one-bank holding companies controlling a substantial part of total commercial bank assets.

Let me briefly develop some implications of these events. Most obvious is the overall pattern of change in which financial intermediaries are growing both more complex and more alike. The universal trend has been particularly evident in the savings and loan industry. Thus, S & L's within recent years have been authorized to accept savings "deposits" as well as savings "shares". Associations can now offer virtually the same line of savings instruments as banks, including, to some extent, certificates in denominations of $100,000 and over. By heavy borrowing from the Home Loan Banks, to which I referred earlier, these once specialized intermediaries are becoming, more than ever before, a kind of diversified intermediated intermediary.

Now, I think that we should applaud appropriate efforts to enlarge the channels through which funds can be raised for relending by these intermediaries, either generally or - to anticipate a point I will develop in a moment - for housing or other pressing social needs. Particularly at times of general monetary stringency, higher-cost funds obtained through the securities market may serve as an efficient supplement to lower-cost funds supplied through savings deposits.

I see no reason, however, why the privilege of raising funds in this manner should be restricted to a relatively few eligible institutions that happen to choose to join the Federal Home Loan Bank System. If it is settled public policy to support selected sectors of the economy, the help of as many types of financial institutions as possible should be enlisted. That is the way to make the most of private expertise, private funds, and private initiative, and it is an obvious avenue of parity between all major depositary institutions.

Again, I applaud the S & L merger and conversion effort to expand the scope of lending and investment powers, including more liberal branching privileges. But I submit that even greater latitude should be provided for institutional initiative by permitting all S & L's and mutual savings banks, at their option, to become broad-scale lenders insofar as federal law is concerned, with common rights and common responsibilities.

During the past few years alone, several S & L's or savings banks have converted to, or merged with, commercial banks. My proposal would help to speed this transition, whether for stock or for mutual institutions.

But particularly illustrative of both the vices of the present system and the unfolding pattern of change into a future one has been the third-party payment system authorized for federal savings and loan associations. As you know, this was the subject of widespread interest - controversy is really the better word - within both the savings and loan industry and commercial banking. The general subject has also been a matter of concern to the Federal Reserve Board, particularly because a number of important economic issues are involved, with implications for the regulation of the banking system, the operation of the payments mechanism, and the conduct of monetary policy.

This episode serves as a dramatic, if unfortunate, example of what can happen under a fractionated regime of depositary intermediaries with divided supervisory authority, at a time when diversification rather than specialization is the order of the day. This kind of competitive brouhaha - a waste of time, effort, and expense - would obviously be eliminated if we had uniform federal chartering and supervision of all major depositary institutions - all capable of accepting demand, time, and savings deposits.

And, finally, the opposite side of the same coin was presented by the recent amendments to the Bank Holding Company Act. Happily, the supervision muddle was not extended to new fields. Rather, the tremendously expanded supervisory powers and functions were placed in the Federal Reserve. The obvious result is that an enormous amount of supervisory unification - more than is generally realized - has already been achieved by something akin to osmosis. The price, however, has been a high one. Anyone who is cognizant of the amount of time now being devoted by the Federal Reserve to a smothering load of supervisory and regulatory problems must wonder how we find time to perform our principal function.

This is a matter that concerns me, too. As I have said many times before, the myriad problems involved in formulating and implementing a monetary policy adequate to cope with things like inflation and unemployment at home, let alone those problems involved in the ever-expanding international activities of American banks, inflows and outflows of Euro-dollars, and the deficits in our balance of payments, already represent more than a full-time job - even in less troublesome times than these. And I can also assure you, on the basis of personal experience, that the task of supervising and regulating financial institutions is likewise a full-time job. That is why I would prefer to see the unification of bank supervision and regulation take place in a different way.

Yet do not misunderstand my criticisms, for I would ask you to see in these five events an essentially organic and interconnected response to the unparalleled demands on our resources at home and abroad, and the resulting necessity of tapping the full potentials of our economy. However piecemeal and ad hoc the episodes may have been, they are essentially steps in the right direction toward a smoothly operating system of depositary institutions gathering savings and allocating credit in open, integrated, and competitive markets.

But, certainly, we are still far removed from this ideal today. Burdened with all too many different statutes and regulations affecting different types of banks, and various types of depositary institutions, we see competitive inequality in the marketplace, unequal treatment among savers and borrowers, and different regulatory and tax treatment of essentially similar functions. And, serving as both cause and effect of this fractionalized system of intermediaries and their balkanized financial markets is a divided set of supervisory authorities.

Overall, this jackstraw heap has inevitably meant increased social costs stemming from the predictable internecine warfare. Typical have been the reactions to the second of my two proposals. Back in 1966, judging from my correspondence, the banks were irate, the S & L's elated. Now positions seem to be reversed. Reportedly, the ABA is favorable and may even propose legislation for this session of Congress to give S & L's the opportunity to convert to commercial banks, but the Savings and Loan League is hostile. I suspect neither the original conclusion nor the subsequent change of position of either part was prompted by the merit of the suggestions but rather the short-term self-interest of the commentators.

But let us not blame the supervised too strongly. The supervisors, too, have their internecine wars. It is a melancholy but undeniable fact that division of power and authority inevitably brings with it the likelihood of needless duplication of effort and of time-consuming, and sometimes fruitless, efforts to harmonize different views of various federal supervisory agencies.

Contrast then the self-evident merit of a uniform system of depositary intermediaries at the federal level, operating under a common set of rules and regulations permitting the widest appropriate range of financial innovation, affording evenhanded and equitable treatment of all depositary institutions, and strengthening the position of the public in formulating and implementing stabilization policies that could be more uniformly applicable.

There would be still more. Hand in hand with the broadest possible latitude to innovate would go freedom to compete on even terms, and yet individual institutions would be free to serve particular segments of local, regional, or national markets where demands for credit prove to be strongest. Benefits of scale in operations as well as other economies of specialization could be realized by any lender as long as particular credit needs seemed most pressing. But the risks associated with undue concentration of assets or liabilities could be minimized, because specialization would not be required. It would not have to persist beyond the time when other credit demands or other means of attracting savings assumed greater importance.

But, as I have already indicated, there is a second circumstance at work in the rising sentiment for unification and standardization in both financial institutions and their supervisory superstructure. This is the increasing concern that we must have a financial framework within which public policies could exercise the widest possible influence in directing credit flows toward branches of the economy judged to be of the highest social priority. To the extent that housing was deemed to be such a sector, for example, appropriate incentives could be offered to encourage all major types of depositary institutions to invest more heavily in residential mortgages. Such a policy would allow maximum response, not from a few specialized institutions holding a limited amount of resources but from all types of lenders drawing savings from the public in deposit form. Indeed, whatever public support was made available for housing in this fashion might be applied against residential mortgage investment by all lender groups rather than, as at present, against certain types of depositary lenders but not against others, whether depositary or not.

Moreover, the extent of direct or indirect public subsidy could be more readily ascertained and weighed openly against competing needs in other sectors of the economy.

Recourse to specialized lending institutions for housing or other special-interest borrowers inevitably produces demands for special protection as well. Once granted - whether in the form of preferential tax treatment, preferential deposit-rate ceilings, or indirect access to the securities market - these measures are likely to fragment the operations of our financial system even further. By limiting certain privileges to a few, many other institutions are overlooked that might use them at least as advantageously to serve the public interest.

Now, these changes I am advocating are far-sweeping. This is evident from the fact that they could ultimately affect all commercial banks and more than 6,000 S & L's and savings banks now operating 5,000 branches and holding assets of over $250 billion - a sum equal to nearly half of the total assets of the commercial banking industry. The successful effectuation of the changes will be dependent upon the development of new expertise. Extensive legislation will be required by the Congress. Drastic reorganization will be necessary to consolidate all federal supervisory responsibility where it should be - in one agency. (Parenthetically, if that single agency were a Federal Banking Commission, such as I have advocated in the past, its members could be readily selected from among the very able men who presently direct the activities of the other three agencies.)

Accordingly, achievement of these goals will take time, even under ideal circumstances. This means that action is called for now.

Bear in mind that this is an age of innovation and boldness. President Nixon has recognized this with his proposal for a sweeping reorganization of the federal government. In addition, his prestigious Advisory Council on Executive Organization, headed by Roy L. Ash, has just issued a report calling for consolidating overlapping federal regulatory agencies in the field of transportation. It is high time that we in the banking field demonstrated that we, too, can shake off the cobwebs and do our part to move our institutions a little closer to the goal of perfection. There are many excuses for inaction, ranging from narrow self-interest to simple inertia. We have a very irrational system of bank supervision and a none too rational banking structure. Even though the case for reform is obvious, we have so far lacked the will to accomplish it. When our young people see this kind of situation they begin to question our ability to conduct our affairs in a rational manner under the present rules.

Consequently, we should begin now to move in a programmed and purposeful plan of advance. As the events of 1970 have demonstrated and as the developments of this new year already show, there is now an almost hydraulic thrust for standardization and streamlining of our organic banking mechanism. The only real issue is how and when this inexorable end-result will come about. It can come about in a long drawn out, piecemeal, random, and agonizing process which reflects the faults of the environment in which it operates and exacerbates those very faults in the short run; or it can do so in a systematic and comprehensive manner with its means chosen and tailored to its ends. And it is to speak for the latter course that today I seek your support and your involvement - so that the idea whose hour has arrived will come to pass in a manner whereby we remain the masters and not the servants of events.