Bk Dir/
Stat
Speeches
FDIC
Misc.
5

NEWS RELEASE

FOR RELEASE P.M.'S TUESDAY, MAY 11, 1971 (5-7-71)

Expanded powers for mutual savings banks probably will require greater accountability and improved standards for selection and tenure of bank trustees, delegates to the 51st annual conference of the National Association of Mutual Savings Banks were told today.

Speaking at the Montreal conference, Irvine H. Sprague, Director, Federal Deposit Insurance Corporation, released a just-completed survey which showed the following characteristics of insured savings banks trustees:

One in five -- 835 trustees -- are over 70 years of age.

Nearly all are selected on a self-perpetuating basis.

Nearly one in four -- 940 trustees -- have interlocking relationships with other financial institutions.

"Most are alert, dedicated, and highly qualified," Sprague observed, "But in the context of today, that is not enough. There should be more access by the younger generations to the power structure to provide the energy and imagination to accommodate to changing times."

Sprague also addressed the problem of capitalizing expanded functions and services of mutual savings banks.

He concluded, "I am confident that your industry has the incentive and the imagination to face up to and solve these problems and when you do, there is little doubt in my mind that the expansion you seek can and will take place."

FEDERAL DEPOSIT INSURANCE CORPORATION, 550 Seventeenth St. N.W., Washington, D.C. 20429 • 202-389-4221

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

FOR RELEASE P.M.'S TUESDAY, MAY 11, 1971

Address of

Irvine H. Sprague, Director
Federal Deposit Insurance Corporation

May 11, 1971

Before the
51st Annual Conference
National Association of Mutual Savings Banks

The Queen Elizabeth Hotel
Montreal, Canada

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

When Grover asked me to wrap up the panel discussion this morning on the topic of modernizing the structure and regulation of financial institutions, it was clear to me that the viewpoints of commercial bankers, mutual savings banks and savings and loans would be more than adequately handled by the previous speakers.

So I will take a somewhat different tack and discuss new legislative procedures that will have an important effect on any decisions to be made in this area.

The legislative ground rules in the Congress have been changed, substantially, since banking legislation was last considered.

A procedural change in voting rules in the House of Representatives for the 92nd Congress will, I believe, have a revolutionary impact on all future legislation of consequence.

Today the votes are being counted -- no longer the anonymous teller and division and voice votes of the past.

For all the years with which you are familiar, banking legislation has been settled in a behind the scenes tug-of-war among commercial banks, savings banks, savings and loan associations and potential competitors, such as travel agents and insurance companies. The public really didn't know what was happening and members of Congress, for the most part, were bored with the subject.

Take a look at the bank holding company legislation that was such a pressing issue with the banking industry. I venture to say that every single issue of the American Banker for nearly a year carried at least one article about bank

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

holding companies. I can't recall a meeting with bank groups when this was not the overriding issue.

Finally, this great debate reached the House floor.

With 435 members eligible, the voting on the amendments that shaped the thrust of this bill was as follows:

63 to 34	97 voting
79 to 25	104 voting
70 to 49	119 voting
50 to 45	95 voting
31 to 28	59 voting
34 to 25	59 voting

This averaged just 89 members voting -- 45 a majority. In addition, there were five voice votes on various amendments.

Then the traditional recommittal motion and finally the vote on final passage:

351 to 24	375 voting

This last vote and the recommittal motion were the only ones recorded. Everything else was anonymous.

It doesn't require a great mathematician to prove that a handful of votes could control on the House floor.

Contrast this with the situation today. The new ground rules put the congressmen on the line with a publicly recorded position on the amendments which determine final form of the bill. Any 20 congressmen can demand a recorded teller vote.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

The first major confrontation under the new ground rules was the SST vote. Here the teller vote on the SST amendment was 217 to 203; one more than the recorded roll call vote on final passage of the entire bill. This total of 420 congressmen voting was a far cry from the old days when less than 100 would be on the floor, and it is safe to predict that the participation will be on the high side from now on.

Since the SST vote the House has had three additional teller votes recorded -- 326, 393 and 388 members participating, and on fairly routine measures.

What does this mean in the context of legislation concerning bank structure and regulation?

To me, it means that more members will take a real interest in banking bills -- that consumer, labor and many other public interest groups will be asking what it means to them -- that many questions never asked before will now be raised.

It would be prudent for the industry to anticipate these questions.

As the previous speakers have indicated -- and the evidence is all in that direction -- we are heading into an era of expanded financial services being offered by all types of institutions. The public will be served, one way or another.

To date, the changes insofar as mutual savings banks are concerned have been small, but the trend is definite. I'm certain it will continue.

To a limited extent, some Delaware, Maryland, Indiana, New Jersey and Vermont savings banks even now are permitted to issue checking accounts to depositors, and there is a great deal of agitation in a number of state

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

legislatures to permit mutual savings banks to offer these services in additional states. Connecticut and Massachusetts are two examples.

Rhode Island savings banks actually own commercial banks and dispense a full range of bank services.

Most of the states with savings banks now authorize some consumer installment lending.

A striking example of the expanded services being offered by mutual savings banks was included in a recent merger application in which the applicant stated: "The services offered by commercial banks are quite comparable to those of .... mutual"; then listed the following services offered by the mutual savings bank:

<u>Service</u>

Passbook Savings
Time Deposits
Automatic Savings
Christmas Club
Personal Money Orders
Travelers Checks
Checks and Drafts
Safe Deposit Boxes
Personal Loans
Auto Loans
Boat Loans
Education Loans
Home Loans (Conv, FHA, VA)
Home Improvement Loans
Contract Collections
Trusts (Limited)
Letters of Credit
Collections
Pay Day Savings
School Savings
Bank-By-Mail
Savings Bonds
Food Stamps

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

As the Congress considers further broadening of the powers and responsibilities of mutual savings banks -- and it will -- you may find a deeper interest developing in how you operate.

I personally believe -- this is not an FDIC position -- that two fundamental questions will be raised and I would suggest you give serious consideration to their resolution.

(1) Who manages mutual savings banks? Who are members of the Boards of Trustees? How are they selected? To whom are they accountable? What other directorships do they hold?

(2) How can savings banks capitalize to meet the growth trends of the future, to meet expanding housing needs, and to meet demands from the expanded areas in which the mutuals might be allowed to go?

Today I will discuss the first question in some detail and pose the second question as something worthy of reflection.

In a survey completed just last week, we identified 4,304 trustees serving 327 insured mutual savings banks in 18 states. These are their characteristics:

A - Nearly one in five -- 19.4 per cent -- was over 70 years of age

B - More than half -- 53.7 per cent -- were over 60 years of age

C - All but a handful were selected on a self-perpetuating basis

(I note the above three characteristics of trustees as facts, without drawing conclusions. What I am telling you today is that others will draw their own conclusions as expanded powers for mutual savings banks are considered.)

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

PROFILE OF INSURED MSB TRUSTEES

No. of Banks	State	Trustees	Over 70	In 60's	Under 60
2	Alaska	29		5	24
69	Connecticut	874	163	291	420
2	Delaware	36	3	20	13
4	Indiana	31	9	10	12
31	Maine	229	54	71	104
5	Maryland	94	26	35	33
8	Massachusetts	230	21	86	123
1	Minnesota	19	2	9	8
30	New Hampshire	335	57	119	159
20	New Jersey	261	51	103	107
120	New York	1,689	347	583	759
1	Ohio	9		2	7
1	Oregon	12	3	2	7
8	Pennsylvania	152	23	49	80
7	Rhode Island	121	33	33	55
6	Vermont	54	15	14	25
9	Washington	99	23	34	42
3	Wisconsin	30	5	9	16
327	18	4,304	835	1,475	1,994

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

In researching for this paper, I found I am not treading on any new ground. The New York Superintendent of Banks in 1966 spoke to the need for improved standards in selection and tenure of trustees and his statistics of five years ago are not dissimilar to those of today. Of course, his comment about the vast majority of trustees still holds. "Most are alert, dedicated and highly qualified by education and experience to carry out the responsibility of their office."

But in the context of today, that is not enough. In considering whether or not to give savings banks expanded powers, the Congress may well want to see a better selection procedure. There should be more access by the younger generations to the power structure to provide the energy and imagination needed to accommodate to changing times. It is also very possible that Congress will want more direct accountability to the depositors in your institutions and they certainly will be interested in where your resources are directed.

Selection of trustees by mutual savings banks is quite different from that found in most business enterprises. I found that with the exception of Ohio, Boards of Trustees are either self-perpetuating or are selected by boards of incorporators which in turn are not open to outsiders. It does not appear that trustees have any real accountability to their members, the depositors. (They, of course, are accountable in court and to state supervisors and legislators.)

In the one mutual savings bank in Ohio, the trustees are elected by the depositors who receive one vote for each $50 on deposit up to a maximum of twenty votes. (In this bank 7 of the 9 trustees are under 60 years of

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

age. Here again, be wary of conclusions. I am told that savings and loan associations that use this formula are not necessarily as well managed as savings banks.)

Already the Congress is addressing itself to the problem of interlocks among trustees.

The proposed Banking Reform Act of 1971 would restrict such interlocks and witness after witness in the past month has testified in favor of some tightening of the rules, including the FDIC, the Federal Reserve, and the Nixon Administration.

Some states have taken action on this question. Massachusetts, for instance, proscribes trustee interlocks with other savings banks, cooperative banks, Federal savings and loan associations, trust companies and National banks. These are subject to certain grandfathering provisions. I understand there is presently pending a bill before the Massachusetts legislature to broaden these proscriptions.

The following table, taken again from the recent survey, shows 940 interlocks -- nearly one in four.

Six hundred and twenty mutual savings banks' trustees hold commercial bank directorships or management positions.

Forty have ties with savings and loan associations.

One hundred sixty eight have ties with an insurance company.

One hundred three have ties with broker dealer.

Nine have ties with another savings bank.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

INTERLOCKING DIRECTORSHIPS OF INSURED MSB TRUSTEES

	Commercial Bank	S & L Assn.	Insurance Company	Broker Dealer	MSB
Alaska	3				2
Connecticut	121	6	34	9	4
Delaware	9	5	6	2	
Indiana	8	1			
Maine	20	6	4	6	
Maryland	31	1	4	5	2
Massachusetts	50	1	11	19	
Minnesota	6		3	1	
New Hampshire	58	1	9	1	
New Jersey	36	5	17	8	
New York	192	13	49	43	
Ohio					
Oregon					
Pennsylvania	22	1	21	9	
Rhode Island	53		5		
Vermont	2		2		1
Washington	9		3		
Wisconsin					
	620	40	168	103	9

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

The press has noted in the past month two developments addressing themselves to the trustee problem that may have altered some of these figures already and probably is a portent of further disaffiliation.

A. Governor Rockefeller has before him a measure restricting close family relationships between trustees and the top five savings bank officials per institution.

B. Officers of at least one of New York's leading commercial banks have announced their resignation as trustees of mutual savings banks.

Now, to the second question, i.e., capital. A recap of the history you all know so well may put the problem in perspective.

The amount of capital funds needed to start a mutual savings bank in the years preceding 1850, when this type of institution was developing in the United States, would appear trivial to us now. During this formative period, the founders of an institution were for the most part philanthropically motivated individuals who would perhaps guarantee the payment of the small amount of operating expenses and interest on deposits for a few years while the bank was becoming established. They viewed the bank as a public service enterprise and the prospective depositors today would be identified as the working poor.

More likely than not business would be transacted after regular hours at a place such as the office of a commercial bank regularly devoted to other purposes. Not infrequently the only piece of equipment owned by the mutual savings bank was a ledger. Thus the rather substantial capital investment that we now associate with a going mutual savings bank and the sizable expenditures for starting business were almost totally unnecessary. The

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

obligations assumed by the founders -- who later on usually became the trustees -- to pay expenses and interest during the early life of the bank and until it became established were not especially burdensome.

Measured in terms of numbers, mutual savings banking reached the crest of development in 1900 when a total of 652 were reported doing business in the United States although their deposits then aggregated only a shade over $2 billion. Since then the number has declined persistently; in 1969 there were 497 mutual savings banks with about $68 billion of deposits. Only 24 have been established in the past 45 years and half of these were conversions from savings and loan associations.

But more important for the purpose of this discussion is the fact that mutual savings banks in the United States now have a very substantial net worth. The combined surplus accounts for these institutions amount to 7.2 percent of total assets at year end 1970, comparing fairly well with the corresponding margin for all commercial banks, both insured and noninsured, which stood at 7.4 percent. Ten years ago the mutuals held an 8.6 percent to 8.0 percent lead in this area.

Mutual savings banks accumulated this sizable margin of capital funds by following the practice over the years of paying their depositors somewhat less than the full amount of earnings on their invested assets in excess of expenses. This was a sound policy to follow because it enabled the banks to accumulate the necessary banking facilities and equipment which they needed to conduct business in the present environment. Furthermore, it provided a necessary margin of protection to absorb unexpected losses and to maintain competitive interest payments when earnings were not sufficient. Worthy of

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

emphasis, however, is the fact that the mutual savings banks did not attract this capital margin from the conventional external sources of investment funds.

What is the situation if mutual savings banks set out to establish themselves in new geographical areas or to enlarge the scope of their activities? Capital funds would be needed to finance expansion.

Where are these funds to be obtained?

This in my opinion is a key question and certainly one deserving serious consideration by the industry as it embarks upon an expansion program.

The accumulation of capital funds through additions to the surplus account has been historically a reasonably satisfactory way for a mutual savings bank to extend its scale of operations over a long period. Of course the rate of growth is slow and it does not facilitate rapid adjustment to changing competitive situations when other types of financial intermediaries with a more flexible capital structure see a profitable opportunity to enter the thrift field -- witness the growth in the savings deposit business of commercial banks and stock savings and loan associations in recent decades. (Of course, if competition increases, deposit growth could slow or even go down, thus obviating any need for capital growth.)

As a practical matter mutual savings banks cannot attract capital funds from investors in the conventional manner. They cannot sell shares of stock as their competitors in the savings field -- commercial banks or the stock savings and loan associations -- to name only two important competing thrift institutions.

What then can the institution of mutual savings banking do to attract capital funds? And without these new funds it is quite evident that the prospects for an enlarged place in the financial structure is not impressive.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Even if the savings banks were to attract very large amounts of new deposits the related additions to the surplus accounts would accumulate much too slowly to finance dramatic extensions in the area and scope of activities.

In some circumstances capital notes or debentures subordinated to the claims of depositors may be used to attract new funds. However, from the investors' viewpoint they may not be especially attractive because the holder cannot participate in future growth if it happens to be profitable -- at best the obligation can only offer a fixed rate of return to the holder. (Nonetheless, I understand some mutual savings banks are successfully using this source of capital today.)

Viewed in terms of the issuing bank, subordinated debt is not as useful as equity funds because the immediate effect of the flotation is to add to operating expenses at a time when the institution needs to obtain funds without this obligation, i.e., during a period when it is experimenting with the development of new business and the profit opportunities are unproved. Furthermore, the use of capital notes or debentures naturally carries with it the long-run obligation to retire the debt.

Please do not interpret any of the above to indicate that either I, personally, or the FDIC has concluded that stock savings banks are the solution. We have reached no conclusions and it may well be that some alternative can be found more in the mutual tradition.

In conclusion, I am confident that your industry has the incentive and the imagination to face up to and solve these problems. And when you do, there is little doubt in my mind that the expansion you seek can and will take place.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis