FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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STATEMENT ON

BANKING AND CONSUMER PROTECTION LAWS AND COMPETITIVE
AND ECONOMIC CONDITIONS WITHIN THE FINANCIAL INSTITUTIONS INDUSTRY

PRESENTED TO

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

BY

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9:30 a.m.
Tuesday, April 28, 1981

5302 Dirksen Senate Office Building

I appreciate this opportunity to testify today on major banking and consumer protection laws enacted by Congress in recent years and on current competitive and economic conditions within the financial institutions industry.

You asked for our comments on the implementation of recently enacted statutes, such as the Depository Institutions Deregulation and Monetary Control Act, as well as possible revisions to that statute or other laws, such as the Financial Institutions Regulatory and Interest Rate Control Act and the Consumer Credit Protection Act. You asked in particular if these laws and regulations enacted in recent years are fulfilling their intended purposes.

You have also requested testimony on the condition of depository institutions, particularly thrift institutions, in these uncertain economic times, and on the impact of money market mutual funds on our financial system.

Finally, in the context of possible legislation dealing specifically with problem or failing depository institutions, you have asked for information about any administrative actions designed to deal with current fiscal problems facing financial institutions.

As Chairman of the Federal Deposit Insurance Corportion, I am pleased to present our views from the standpoint of the federal insurer of the people's deposits and the deposits of business, charitable groups, governmental units and other entities, in some 15,000 banks throughout the United States. The FDIC is also the primary federal supervisor of some 9,300 State-chartered banks that are not members of the Federal Reserve System.

I want to say first of all that our system of federal deposit insurance is strong. Our insurance fund continues to grow and is more than adequate for any foreseeable eventuality. Our corps of skilled, highly trained and dedicated employees remains committed to our statutory mandate to promote the safety and soundness of the banking system. The people of America can continue to bank with confidence.

Despite the growing demands and the increasing complexity of workload, we at the FDIC are carrying out our duties fully and much more efficiently than the government as a whole. In 1979 our administrative expenditures increased just 3.4 percent, compared to 9.5 percent government wide. In 1980 our increase was 10.7 percent, compared to 17.3 percent throughout government. In 1981 to date we are running below our projected expenditures.

Our lean, tight dedicated operation with 3,500 employees is making no sacrifice in quality. One of the reasons for the success is our divided examination program, which has been

greatly expanded these past two years in cooperation with individual States and about which I will have more to say later. Another is the conscientious effort of our FDIC people to reduce travel expenditures and save fuel. Our staff will travel an estimated 16 million miles to carry out their bank examination duties in 1981. This is a reduction of 12 percent from 1980, which was itself a reduction of nine percent from 1979. We are able to achieve this savings by more careful scheduling of examinations and by more efficient car pooling and a spirit of cooperation from our workforce.

We have not -- nor do we intend -- to cut back on our visits to banks. In 1981 we will conduct 5,800 safety and soundness and 6,400 compliance examinations.

The insurance fund now exceeds $11.3 billion and is increasing. Net income last year topped the billion-dollar mark for the first time with a record $1.2 billion gain. This year we project net income of $1.3 billion. We also are entitled to a $3 billion draw on the Treasury, if needed.

Three banks have failed to date in 1981, about the same rate as recent years. Deposits of failed banks totaled $75 million so far this year, compared with $215 million for the 10 failed banks in 1980 and $112 million for the 10 failures of 1979. In the majority of cases failure resulted from internal factors related to management, fraud, or similar circumstances unrelated to the economic environment. There are no detectable trends to relate bank failures to the general condition of the economy.

Problem Banks

The number of banks on our problem list continues to decline despite the economy and the well publicized problems of the thrift industry. As of March 31, 1981, 204 banks of all types were on the list, down from 217 banks at the end of 1980 and 287 banks at the end of 1979. The problem list contains a built-in lag, since it is usually 18 months or more before poor conditions in the economy magnify the weaknesses that cause banks to go on the problem list. Any effects of the unfavorable interest rate cycle that began in the last half of 1979 and continues today might not be reflected in the problem banks' list until some time later.

The Commercial Banking System in 1980

The year 1980 was marked by substantial turbulence in the nation's economy and credit markets. Output and employment declined substantially in some vital sectors of the economy. The housing and auto industries were particularly hard hit. Inflation, as measured by indexes of consumer and producer prices, continued to soar at double-digit rates. These developments in the economy contributed to instability in the financial sector, as reflected most notably in the movement of interest rates.

The pattern of interest rate changes last year was unprecedented in recent history, both with respect to the magnitude and frequency of change. The prime rate, for example, rose from 13.25 percent to a record 20 percent, declined to less than 11 percent and ended the year at a new record level of 21.5 percent. These wide fluctuations and the unprecedented levels to which interest rates rose imposed stresses on the economy and the banking industry. The high interest rates contributed to a substantial growth in money market mutual funds during the year. Nevertheless, commercial banks as a whole made some progress, as shown by median growth figures and values of selected performance ratios.

Total assets of all insured commercial banks grew approximately 10 percent in 1980, almost as much as in 1979. This growth was more expensive to fund, however, as interest rates rose substantially and deposits at commercial banks shifted from relatively low cost, fixed ceiling instruments, (e.g., passbook savings, fixed-ceiling time deposits and NOW accounts) to instruments with market-related ceilings (e.g., six-month money market certificates, small saver certificates, and large negotiable CDs). These more expensive instruments increased from 55 percent of interest-bearing liabilities at all commercial banks at year-end 1979 to 68 percent at the end of 1980. Furthermore, this deposit shift has been more dramatic at smaller banks (less than $100 million in assets). For these banks the percent of interest-bearing liabilities in deposits without fixed ceilings increased from 35 percent at year-end 1979 to 58 percent by year-end 1980. The percentage for larger banks increased from 60 to 71 percent over the year. Banks were able to offset higher cost of funds and increased noninterest operating expenses by generating even higher operating revenue so that net income after taxes still increased.

Earnings

Net income of insured commercial banks grew by 14 percent in 1980, while total assets grew by ten percent. Thus, the median ratio of net income to average assets was 1.20 percent, up slightly from 1979. As in the past, earnings were inversely related to asset size, ranging from a return on assets of 1.28 percent for banks under $25 million in size to .63 percent for banks over $5 billion. Only banks of over $5 billion experienced a growth in assets exceeding their growth in net income.

Liquidity

The liquidity of the commercial banking system improved in 1980, but with some offsetting developments. One measure of the overall pressure on liquidity is the ratio of temporary investments (mainly federal funds sold and securities maturing in less than one year) to rate-sensitive purchased funds (mainly federal funds purchased and time deposits of more than $100,000). As of year-end 1980 this ratio was 135 percent as compared to 107 percent at year-end 1979, a liquidity improvement of 25 percent. There

were large differences in this ratio for banks of different size -- the smallest size group had a ratio of 180 percent and the largest category 34 percent -- a continuation of the 1979 pattern.

This overall improvement in the liquidity position of banks was offset somewhat by shifts in the deposit structure to proportionately more short-term instruments. At the end of 1980, six-month money market certificates, passbook accounts and large certificates of deposit, most of which had maturities of six months or shorter, constituted 53 percent of all domestic deposits in commercial banks. When demand deposits are included, 90 percent of all bank deposits might be subject to withdrawal in six months or less. This is up two percentage points from the end of 1979. For banks of under $100 million in assets, the ratio was 83 percent, up five percentage points from 1979. The ratio was 92 percent for large banks, up two percentage points from last year.

Asset Quality

For all bank size categories, asset quality appears to have decreased somewhat while loan loss reserves have increased slightly to counter this development. Weakness in the economy apparently had an impact on loan losses which rose in 1980 by 40 percent over 1979. However, this increase in loan losses was lower than occurred in the 1974-1975 recession (net losses increased 69 percent in 1974 and 66 percent in 1975).

Capital Adequacy

The ratio of average equity capital to average assets for all insured commercial banks increased from 8.06 percent in 1979 to 8.27 percent in 1980. In general, an increase in this equity ratio occurred for banks of under $1 billion in assets. The equity capital ratio was about the same as in 1979 for the banks in the $1 billion to $5 billion group, but decreased 18 basis points to 4.28 percent for banks of over $5 billion.

Regional Directors' Comments

This analysis takes into consideration comments of our 14 Regional Directors. I asked each one to assess the potential impact of local economic conditions on banks in their regions. In addition to the general concerns, including those for thrifts and competition from the nonregulated sectors, our Regional Directors cited local economic developments that might affect banks.

Our Regional Directors in the Midwest report that adverse conditions in the automobile and related industries are already causing noticeable problems for some banks. Several Regional Directors responsible for agricultural areas expressed considerable concern about poor crop conditions caused by adverse weather

conditions. Poor crop years usually mean additional pressure on farm area banks, particularly in terms of loan demand and loan repayment. Traditionally, federal farm lending programs have been a source of significant relief. Now, however, the prevailing concern in these areas is that continued poor crops coupled with any major cutback in farm programs would exert substantial additional pressure on some banks. Some Regional Directors expressed concerns about problems stemming from the depressed housing industry and possible declines in real estate value.

Overall, Regional Directors were concerned that certain circumstances could cause problems in selected areas, but all Regional Directors believed that problems would be manageable.

In summary, the commercial banking system emerged from 1980 without serious problems and with some improvement in its overall condition. This occurred despite the wide swings in interest rates which have focused attention on the potential exposure of banks to interest rate risk. Banks with deposits of less than $100 million have generally been considered more vulnerable to interest rate swings than large banks. These smaller banks have experienced a larger shift in liabilities from low cost savings and other deposits to expensive and market-sensitive money market certificates. However, smaller banks generally performed well in 1980. In fact, their performance in the areas of earnings, liquidity, and capital exceeded that of the larger sized institutions. Apparently the ability of small banks to adjust asset portfolios was greater than many had anticipated.

The improvement in the condition of the commercial banking system in 1980 does not necessarily imply that similar satisfactory results will emerge in 1981. We must remain alert to any continued instability in the economy, further competition for bank and thrift funds from the nonregulated sector of the money market, and the weakened condition of other types of regulated financial institutions which will test the capabilities of bank managers, regulators, and legislators throughout the year.

Mutual Savings Banks

The inflation and accompanying high interest rates that have dominated the economy over the past few years have created serious problems for the mutual savings banks that are supervised and insured by the FDIC. Higher interest rates have significantly increased the cost of savings bank deposits. While yields on their earning assets have risen, they have done so much more slowly than deposit costs. Assets are heavily concentrated in long-term, fixed-rate mortgages and bonds which turn over slowly. The problem has been exacerbated by slow deposit growth resulting from a low personal savings rate, the diminished appeal of taxable, fixed-return investments, and increased competition from money market funds and market instruments. These conditions have severely limited savings banks' ability to acquire higher yielding assets.

Last year, FDIC-insured mutual savings banks in the aggregate lost money. The loss amounted to about 0.17 percent of average assets compared with net income of about 0.45 percent of assets in 1979 and 0.59 percent in 1978. The loss was not evenly spread throughout the country. New York City savings banks, which account for about 40 percent of the deposits of FDIC-insured thrift institutions, lost about 0.62 percent of average assets last year. However, the rest of the industry had net income of about 0.17 percent. The weaker performance of many of the New York City savings banks reflects a combination of factors, including past restrictions on permissible lending, past restrictive usury ceilings, unfavorable State and city tax treatment, a relatively static mortgage market, and a high degree of competition from large money center institutions and money market funds.

Even if interest rates decline moderately over the next year or so, deposit costs at savings banks are likely to increase as deposits continue to shift out of passbook accounts and as lower rate certificates mature and either leave the institutions or roll into much higher cost instruments.

If interest rates decline markedly and remain lower for a sustained period, most savings banks should be able to adjust portfolio returns to bring them into line with the market and make appropriate adjustments to attain a profitable position. Savings banks then would have the opportunity to take advantage of the the broadened lending powers authorized under the Monetary Control Act of 1980 and State laws to reduce their exposure to future interest swings. Thus far, prevailing financial market conditions and other factors have made it difficult for savings banks to take advantage of these broadened powers to any significant degree. If unfavorable conditions persist in financial markets for a prolonged period, then some savings banks are likely to need assistance if they are to continue to operate. The FDIC has the capability of providing that assistance should such action be considered necessary and appropriate.

Your letter of invitation to testify made reference to the expected submission of proposed legislation dealing specifically with problem or failing depository institutions. Last year the five regulators, acting unanimously, submitted to the Congress a bill that would provide certain emergency authority in this area. I still believe that a bill along the lines of S. 2575 of the last Congress is needed to provide us with additional tools should the need arise. It admittedly poses tough questions for you in the Congress -- should we provide a subsidy with unknown but potentially large budget impact; should you break the state barriers to holding company acquisition of all types of institutions, even on the limited basis of a very large closed institution? As a realist I know such a bill cannot pass without active Administration support. Meanwhile, a high level task force I designated last year has been in continuous action since December,

analyzing in depth all of our troubled thrift institutions, so we will be positioned to act to the extent our present authority allows, should the need arise.

Money Market Mutual Funds

A major financial development in 1981 which has significantly affected depository institutions has been the tremendous growth of money market mutual funds. Total fund assets stood at more than $115 billion on April 8, 1981, having increased by more than $40 billion, or about 55 percent, since the start of the year. The number of shareholders in money market funds has grown to more than 5.5 million.

This rapid growth has likely had the greatest adverse impact upon thrifts and small commercial banks. The interest-paying household deposits on which these institutions depend for the major portion of their liabilities are the very deposits which are most subject to disintermediation in periods of high and rapidly rising interest rates, especially with a negatively sloped yield curve and deposit rate ceilings. Further, it is extremely difficult for thrifts and small commercial banks to recapture money lost to money market funds by issuing large certificates of deposit. Money market funds are more likely to purchase the certificates of deposit of the very large commercial banks and to invest in commercial paper and other instruments.

This activity amounts to a substantial reallocation of funds, very likely to the detriment of home mortgages, agriculture and small business. Funds which otherwise would be used for these purposes in their local communities would seem to be escaping to national money markets. Such a diversion of funds from local depository institutions also can lead to earnings and liquidity problems for such institutions. Of particular concern to us is the heavy impact on small banks and mutual savings banks.

With the data currently available, it is impossible to provide exact figures on the diversion of funds from institutions to money market funds, but we believe that the diversion from thrifts in recent months has been substantial. Shares in money market funds are close substitutes for time and savings deposits at institutions, and one would expect the rational consumer to shift funds from low yielding and/or relatively less liquid deposits into the higher yielding, more liquid money market funds. Indeed, a survey conducted by the Unidex Corporation in June of 1980 revealed that 56 percent of the money invested in money market funds by the respondents of the survey came from either regular savings accounts or certificates of deposit.

Various proposals have been made to reduce the relative attractiveness of money market funds vis-a-vis instruments at depository institutions, but it is going to be difficult for you

to enact remedies which would reduce the investment returns to many consumers. Full hearings on this issue will help to clarify the competing interests and determine whether government action is appropriate.

IMPROVEMENT IN BANK SUPERVISION

Bank examination is the heart of our supervisory program to promote the safety and soundness of the banking system. The FDIC will continue to exercise a strong bank examination function. I have concentrated these past two years on fostering State-FDIC cooperation, both because it makes sense and because it is a necessity in coping with burgeoning workload within the constraints of severe budget and manpower limitations, both on the State and Federal levels.

Today we participate with 18 States in divided examination programs covering 3,200 banks, about one-third of all those we supervise. Negotiations for divided examination agreements with additional States are in progress.

In all my years of government, never have I seen a program do so much, so well, so fast. The returns in economy and efficiency for both the States and the FDIC are enormous and the benefits to the covered banks in reduced burden are substantial. The Federal Reserve Board, after reviewing our results, recently voted to adopt a similar program, so all State-chartered banks are now eligible.

The concept is simple: the FDIC and the States jointly identify banks not of supervisory concern and divide them equally for the purpose of examination. The State examines one-half, the FDIC the other, and we exchange reports. The next year we switch halves.

Yesterday in Houston I announced to the Conference of State Bank Supervisors a new element to accelerate our momentum: starting immediately, the FDIC is offering free of charge "road show" education classes to examiners of States in the divided examination program.

We will work with the States, tailoring classes to meet their needs and scheduling classes at locations convenient to the State examiners and cost-effective from a travel standpoint. Our motive is simple: since we rely on State examinations in the divided examination program, we have a stake in the best trained State examination force possible.

The keynote of the divided examination program is flexibility. There is no single, rigid nationwide structure to which all States must conform. States negotiated with us on cooperative efforts of various kinds that suit their individual needs and accommodate the needs of the FDIC. The program is voluntary. It is open to all States which meet examination standards and other qualifications.

By conducting fewer examinations, both the State and FDIC conserve resources which can be used to focus on our other responsibilities. Well managed banks are less burdened by examination. Banks with problems receive the same or even increased attention by the State and the FDIC through our joint supervisory efforts. In this way, we are able to maintain our vigilant supervision of problem institutions and relieve the burden on the great majority of our banks which are well managed and sound.

We are undertaking other initiatives. Last year at my direction our Division of Bank Supervision reviewed all FDIC application forms, seeking ways to reduce the information requests to essentials. The Division developed shortened core application forms for joint use by FDIC and the State so that a bank need complete only a single form. We print such forms and supply them free to States. Seventeen States now participate; 11 more are likely soon, and we are looking for more. Our Regional Directors also work with States to coordinate investigations and other application routines. We delegate much of the approval authority to the Regions to speed up the process.

In another cooperative program, 10 States have computer terminals that tap into the FDIC's data base that is open to divided examination States. These States have immediate access to key financial and structural information on banks they supervise. Forty States annually receive the FDIC's Comparative Performance Report, which provides both trend information and peer group comparisons for insured nonmember banks.

In 44 States, the State Commissioner and FDIC participate jointly in some or all enforcement actions.

States in the divided examination program may have their examination reports typed at no charge at our four Regional Typing Centers in Minneapolis, Omaha, Kansas City and Dallas. This is designed to help get a completed typed examination report back to the bank faster.

Depository Institutions Deregulation Committee

The Depository Institutions Deregulation Committee (DIDC) was established on March 31, 1980, by Title II of the Depository Institutions Deregulation and Monetary Control Act of 1980. The FDIC Chairman, along with other DIDC members, the Secretary of the Treasury and the Chairman of the Federal Reserve Board, the Federal Home Loan Bank Board, the National Credit Union Administration, and the Comptroller of the Currency who is a nonvoting member, are committed to the objective of phasing out interest rate ceilings at the earliest practicable date. Interest rate controls which once served a useful purpose have proven to be anticompetitive, have discouraged savings, have been inequitable to small savers, and have caused disruption in financial and housing markets. While we wish

to eliminate these inefficiences at the earliest practicable date, it is important to balance these goals against inimical effects on the banking and thrift industries if interest rate deregulation is brought about too precipitously. Congress recognized this fact by providing a six-year time period to phase-out interest rate ceilings and provided a nonbinding intermediate target schedule for increasing maximum allowable rates on passbook and similar savings accounts.

The task of deregulating interest rates has not been easy, particularly in view of the turbulent interest rate environment of the last year or so and the virulent competitive pressures in the 1980-1981 financial environment. We have not been lacking in conflicting advice on how to proceed.

The DIDC has made a concerted effort to place financial institutions on a competitive footing with other entities which are competing for the public's available funds. DIDC actions on money market and small saver certificates sought to bring rates paid on those instruments more in line with other investment alternatives. The actions were intended to have the collateral benefit of providing the public-at-large with something closer to a market return on their savings. However, the actions have not directly addressed the money market fund competition discussed earlier.

At its meeting on March 26, 1981, the DIDC voted to issue for public comment a schedule for decontrolling various types of deposits on a gradual basis starting with longer-term deposits of five years or more on July 1, 1981, and culminating with elimination of all ceilings on April 1, 1986.

In a simultaneous action, the Committee proposed for public comment the removal of the 11.75 percent and 12 percent interest rate ceilings which apply to commercial and savings banks, respectively, on 2-1/2 year or longer small saver certificates. This change would allow the permissible rate on these instruments to reflect actual market values as measured by the 2-1/2 year average yield on Treasury securities. I expect we will act on these two proposals in early June.

The legislated differential for thrift institutions will disappear with the completion of deregulation, but, for now, the differential is essential for the continued viability of the thrift industry. Ultimately, the needs of the depositing public must be served, and the thrift industry must expect to compete without the benefit of government protection.

FFIEC Accomplishments

The Federal Financial Institutions Examination Council (FFIEC) was established on March 10, 1979, pursuant to Title X of the Financial Institutions Regulatory and Interest Rate Control Act of 1978 (FIRIRCA). The FFIEC is composed of five members of

the five federal agencies with regulatory and supervisory responsibility over federally chartered or insured depository institutions; i.e., the Comptroller of the Currency, a member of the Federal Reserve Board, the Chairman of the Federal Home Loan Bank Board, the Chairman of the National Credit Union Administration Board and the Chairman of the FDIC. Our State regulatory counterparts are represented through a State Liaison Committee.

The FFIEC already has a number of accomplishments to its credit: a uniform rating system for financial institutions; a policy statement on coordination of bank holding company inmspections and subsidiary lead bank examinations; a policy statement on supervision of U.S. branches and agencies of foreign banks; a uniform supervisory policy for the classification of delinquent consumer installment loans; standardized instructions for the quarterly reports of condition and income filed by U.S. commercial banks; uniform guidelines on internal control for foreign exchange activities in commercial banks; a new "Policy Guide" for the Truth in Lending Act, as amended; an interagency supervisory policy regarding the assessment of civil money penalties; a uniform bank performance report; a uniform consumer compliance rating system; elimination of the "Report on Security Devices"; and uniform examination procedures under statutes governing community reinvestment, electronic fund tranfers and financial privacy.

In our judgment, the FFIEC is performing usefully, but at a very high cost in terms of agency resources. It is too early to determine whether the FFIEC is more effective and efficient in promoting uniformity in the supervision of financial institutions than some form of agency consolidation might be.

The FFIEC has had a positive impact on the representative agencies; it has made for more open lines of communication between agency principals, as well as agency staff members. On the negative side, the FFIEC's frequent Subcommittee and Task Force meetings have been a tremendous drain on high level staff of all agencies.

LAWS AND REGULATIONS

You have asked us specifically to comment on the implementation of recently enacted statutes, such as the Depository Institutions Deregulation and Monetary Control Act, as well as possible revisions to that statute or other laws, such as the Financial Institutions Regulatory and Interest Rate Control Act and the Consumer Credit Protection Act.

We are opposed to excessively burdensome regulations. Two years ago I established a regulatory review committee within the FDIC to deal with unwarranted regulation. Essentially, all

proposed regulations now must go through an internal procedure monitored by the Board of Directors and designed to ensure that the new regulation is needed and that it is the minimum to get the job done. The procedure gives special consideration to the effect on small banks and ways to avert undue hardship. Second, the committee has reviewed existing FDIC regulations for the same purposes. We have been successful in eliminating six regulations altogether, reducing and simplifying eight others and changing one from a regulation to a policy statement. Four of our regulations currently are being reviewed for possible simplification.

We welcome your Committee's comprehensive review of the law and regulation affecting the financial industry.

Before I come to our specific comments, let me say first that in any review it is important not to lose sight of the real cause and necessity for many provisions of existing law. We must not make the mistake of confusing poor administration with poor policy or law. We do not want to turn the clock back; we need to make it run better. There was at the time of enactment -- and there continues to exist today -- a real need for laws expressing the public policies that we are commenting on today.

In the late 1960's many lenders were charging one interest rate for loans and advertising a lesser rate. That's why we have Truth in Lending.

Some banks were not serving the financial needs of their local communities. That's why we have the Community Reinvestment Act and the Home Mortgage Disclosure Act.

Some insiders were taking advantage of their positions to obtain loans from their own banks or correspondent banks on far more favorable terms than were available to ordinary borrowers. That's why we have the Financial Institutions Regulatory and Interest Rate Control Act.

Some banks were discriminating in their home mortgage and other lending policies. That's why we have the Fair Housing Act and the Equal Credit Opportunity Act.

In each case, the need was and is genuine. The basis for the law is valid. But if a good law is encumbered by lengthy, complex and sometimes inappropriate provisions -- either in the regulations and interpretations or the statute itself -- and if the agencies lack flexibility in implementation, then we have a problem.

I meet frequently with bankers' groups and I can assure you that they make their feelings known to me about complying with laws and regulations. In many instances, these are legitimate complaints. But it is not unusual to find that the banker simply does not like the law.

I do not think that complaints of poor administration should be used as an excuse to repeal the hard-won gains of the last decade and a half for consumers and minorities and women and others who have benefited from these laws and the public policies they represent.

With that preface, let me say that I wholeheartedly support changes that will facilitate administration of these laws. We want changes that will let us do our job better with less burden all around.

What is needed is to critically re-examine each statute and each regulation to determine if they are clear enough to be easily understood and flexible enough to permit common sense and even-handed enforcement without imposing unreasonable burdens. Some of what is needed can be done administratively. Other aspects will require modification of law. We stand ready to work with our partner regulatory agencies and with the Congress on a regulation-by-regulation and law-by-law basis.

One of the most fruitful avenues we can pursue legislatively is to find where we can institute cutoffs for banks -- usually small banks -- not heavily involved in the activity a given law seeks to regulate. In too many cases today, the small hometown banker who does only a small amount of a given line of business is held to requirements designed for large institutions which have legal departments of their own to decode the issuances from Washington and figure out countermoves. The small bank, which may have only a few people in the entire office, cannot cope with the pages of "simplification" and explanation and instruction put out by the regulation writers in Washington. Here is one area ripe for relief.

Now, then, let me turn to specifics -- changes that will permit us to do a better job of carrying out the intent of the law without affecting the principle underlying that law.

Our staff has made a thorough review of laws and regulations of the past 15 years. In addition, we have worked with the Federal Financial Institutions Examination Council on its interagency review of the Financial Regulatory and Interest Rate Control Act. We have several recommendations and comments.

First, we recommend enactment of the changes in FIRIRCA that the FFIEC submitted to Congress earlier this month. Essentially, these changes, as they would affect insured State nonmember banks, would clarify FDIC authority in administering civil money penalties, eliminate the requirement that bank loans to insiders in excess of the $25,000-aggregate maximum be approved by a majority of a bank's board of directors and would allow bank boards to establish committees to approve such loans, limit bank recordkeeping of insider loans to its own insiders and exclude those of other subsidiaries

of the same bank holding company, make appropriate exemptions from insider lending restrictions and reporting requirements for foreign banks, clarify FDIC authority to remove management officials in enforcement of the Management Interlocks Act, and permit bank insiders subject to the reporting of loans from correspondent banks to compute their total indebtedness 30 days prior to a reporting date instead of 10 days.

Second, we believe the Truth in Lending Act and its voluminous regulations and interpretations could stand a major overhaul, but are recommending only one change at this time in view of the major revisions enacted one year ago and the amended Regulation Z promulgated one month ago. Our Regional Directors cite Truth in Lending as one of the most onerous laws to enforce. Banks have not been hesitant to make their feelings known. But we believe the best course now is to gain experience under the revised statute and regulations before we consider wholesale changes, which should be prefaced by extensive hearings.

The limited immediate change we are proposing involves reimbursement provisions under the Act. The statute and regulations spell out so many exceptions and special circumstances that they require substantial examiner time to review and are difficult for banks to understand. Our record of the proper use of flexibility in the safety and soundness area would support the granting of similar flexibility in the Truth in Lending reimbursement area. Section 108(e)(2)(D) is too narrowly drawn to permit the regulatory agencies appropriate discretion in applying the reimbursement remedy in a manner they deem equitable in individual violations of the statute.

A related problem goes to Section 108(e)(3)(A), which allows reimbursements for violations to be spread over a period of time if immediate full adjustment would have a significantly adverse impact on safety and soundness, is not effective in dealing with a capital adequacy problem. Even though the payments may be spread, the entire adjustment must be shown in the first year so that the full impact on capital adequacy is reflected.

We recommend early action to grant the regulatory agencies appropriate flexibility in determining whether reimbursement is necessary or justified.

Third, we believe that the Community Reinvestment Act has had significant beneficial effects in its two years of operation and suggest that Congress may appropriately wish to hold comprehensive oversight hearings on its application. The FDIC was the first agency to deny an application on CRA grounds. We believe that that action in 1979, and others that followed it, by the FDIC and other regulators, let the industry know that we regulators would enforce CRA. It made bankers review their lending operations accordingly. Questions that might be considered during any

oversight hearings may concern geographic coverage of the Act -- might it be limited to urban areas -and the function of the regulators -- should we be required to assess a bank's community lending record only when the bank makes an application. This latter change would eliminate the assessment as part of a routine bank examination; it would save examiner hours and focus our resources on a bank's community lending record at the time when we have authority to impose a sanction.

Fourth, we recommend that the International Banking Act of 1978 be amended to require that if a foreign bank seeks and obtains deposit insurance for one branch in a given State, it must do so for all branches in that State unless excepted by the FDIC. The purpose is to prevent confusion in the public mind as to whether a given branch of a foreign bank is insured. Statewide insurance would limit foreign bank's ability to shift deposits from an insured to an uninsured branch to the detriment of depositors and, possibly, to the detriment of the FDIC whose deposit insurance assessments may be levied only on the deposits in insured foreign branches. Further, statewide insurance would relieve a competitive disadvantage now visited upon domestic banks which cannot establish uninsured branches and must pay deposit insurance assessments based on total deposit liabilities in all branches. We also recommend an amendment to provide that confidential information about foreign banks submitted by foreign bank regulators or the banks themselves not be subject to mandatory disclosure under the Freedom of Information Act. This would assist the FDIC in overcoming the reluctance of foreign banks under present circumstances to provide the FDIC with confidential information for insurance purposes.

Fifth, we recommend an amendment to the Privacy Act of 1974 that would clarify our authority to prevent inadvertent disclosure of information about persons that may be contained in a file maintained under the name of another individual.

Sixth, we note an inconsistency in the error resolution provisions of the Fair Credit Billing Act and the Electronic Fund Transfer Act and suggest that the Congress may wish to reconcile them. The inconsistency causes additional burden on banks that offer debit and credit cards or a combination debit/credit card. Under the Fair Credit Billing Act, a bank has up to 30 calendar days to take action or resolve an alleged error; under the Electronic Funds Transfer Act, the time limit is 10 business days. Institutions offering combination credit/debit cards are subject to both Acts for the same card, and under some circumstances may have to meet inconsistent requirements. Furthermore, the Electronic Fund Transfer Act and its implementing Regulation E are extremely broad and complex. Our Regional Directors point out, for example, that the regulation covers banks whose only transfer activity is the direct deposit of Social Security checks. Our experience indicates that this law and regulation have the potential to become complex and onerous; for that reason we believe a comprehensive legislative review of this area would be appropriate.

Seventh, we recommend that the National Historic Preservation Act of 1966 be amended to except federal actions, such as determinations on applications, that may occur only after the State has acted on the applications. This would leave the determination of historic preservation to State and local processes. At present, the law requires the FDIC and other agencies having the authority to authorize any undertaking to consider the effect of the undertaking on any district, site, building, structure or object that is included in or eligible for inclusion in the National Register.

Eighth, we recommend amendments to the Home Mortgage Disclosure Act that would permit us to achieve about the same level of reporting on the distribution of home mortgage lending while relieving the burden on smaller banks. The coverage test for bank reporting on mortgage loans should be changed to reflect the size of the bank's mortgage and home improvement loan portfolio rather than the bank's total assets. Further, the requirement for aggregation of HMDA statistics should be changed to begin with reports for calendar 1981 rather than 1980. We also suggest that Section 310(a) be amended to delete the requirement related to aggregation of lending patterns in census tracts grouped according to location, age of housing stock, income level, and racial composition. A substitute for this provision could be a requirement to aggregate for each SMSA, lending patterns by census tract (or county) and to report for each tract (county) information on age of housing, income distribution, and racial composition. This would be a more flexible way for the public and regulatory agencies to seek desired information and would be cost-saving to the agencies.

Ninth, we recommend that the Bank Holding Company Act, which now also applies to one-bank holding companies, be amended to provide that the supervisor of the lead bank will supervise the holding company. At present, the Federal Reserve exercises supervisory authority in all bank holding companies, even when no member banks are involved.

We would like to comment on our experience under the Flood Disaster Protection Act of 1973. Under the law, we have issued our Part 339 regulations prohibiting banks we supervise from doing any lending secured by improved real estate or a mobile home located, or to be located, in a designated flood hazard area when flood insurance is available under the National Flood Insurance Act, unless the security is covered by appropriate flood insurance. Our regulation also requires each bank to maintain sufficient records to show how it made its determinations on loans and to issue notices to borrowers about special flood hazard areas and the availability of federal disaster relief assistance. In the past, one major problem was the availability of good maps identifying flood hazard areas. The Federal Emergency Management Agency sought to establish a central clearing point on flood status of property and whether the community is participating in the national

flood insurance program; however, the clearing point project has been terminated due to budget constraints, and lenders face the difficulty of complying without current, legible and readily accessible maps. In recent years, lawsuits have raised the issue of whether the Act provides a basis for private right of action against financial institutions which fail to comply. The statute and legislative history are silent on the point, but the possibility exists of substantial civil litigation in the event of a major flood disaster.

We have no legislative recommendations to make concerning the Fair Credit Reporting Act, the Equal Credit Opportunity Act, the Fair Housing Act, the National Environmental Protection Act, the Currency and Foreign Transactions Reporting Act of 1970, the Regulatory Flexibility Act of 1980, or the Paperwork Reduction Act of 1980.

Finally, we are continuing to reviewing FIRIRCA to see if at some future time further amendments should be proposed.

Areas at which we are looking include the following:

Whether Section 22(h) should be amended to extend the prohibition on payment of overdrafts to include principal shareholders and the related interests of directors, executive officers and principal shareholders (present law covers only individual accounts of directors and executive officers),

Whether insider loans fully secured by certificates of deposit, savings accounts or equally acceptable collateral should be exempted from the Section 22(h) loan ceilings,

Whether Title II, Depository Institutions Management Interlocks Act, should be amended to permit civil money penalties,

Whether Title VIII, which amends the Bank Holding Company Act Amendments of 1970, should be clarified to indicate whether its prohibitions on insider correspondent lending and accompanying insider reporting requirements should apply to mutual savings banks; and whether the provision requiring banks to report to the appropriate supervisory agency on insider correspondent borrowing should be eliminated,

Whether reports on loans to a bank's insiders and to insiders of correspondent banks required by Title IX to be made to the federal supervisors and to be publicly available should be eliminated; the reports do not appear to be effective as a public disclosure mechanism or a supervisory tool; the reports deal in aggregates, do not include loans to directors and do not permit one to distinguish between nominal and heavy borrowers; and

Whether Title XI, the Right to Financial Privacy Act of 1978, should be amended to (a) permit the free flow of information

among the federal financial supervisory agencies, (b) give agencies express authority to notify law enforcement agencies of crimes that may affect bank safety and soundness without giving the customer notice, (c) define the term "notice", (d) clarify whether the Securities and Exchange Commission is a supervisory agency under the Act, and (e) require that the requesting federal agency, rather than the transferring agency, give notice to the customer after the requester obtains the customer's record.

We are continuing to evaluate our experience under Title VI, Change in Bank Control Act, and have no amendments to recommend at this time. However, we believe that this Act has had substantial beneficial effects that cannot be fully measured. The Act gives the FDIC and other regulators a useful veto on bank takeovers by undesirable interests; we believe that the law's existence itself has inhibited such interests in even attempting to gain control of banks. We undertook a comprehensive account of our experience under the Act in the statutorily mandated report which was submitted to the Congress March 10, 1981, and we would commend the report to your attention.

In closing, I thank your committee for this opportunity to state our views and commend you for the exercise in oversight that you are embarking on today.