

SUPERVISORY LEADERSHIP IN THE  
AMERICAN BANKING SYSTEM

Address of

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Six years ago, at my first NASSB Convention, there were many who despaired for the future of state-chartered banking and for the decentralized banking system which is at the heart of the nation's financial structure.

State-chartered commercial banks had become restless and impatient as they watched a resourceful and determined Comptroller cut through the provisions of Federal and state law that previously had been thought to restrict the activities of national banks. Mutual savings banks, then as now limited to a state charter, were beginning to make headway on their proposal for a Federal charter option, while large numbers of state-chartered savings and loan associations continued to exercise the option they already had. In a regulatory structure so conducive to local responsiveness and to innovation at the state level, it was obvious that state-chartered banking, at least to many of those most directly concerned, was not living up to its possibilities or meeting the challenges required by technological change and an increasingly competitive marketplace.

Today, this description no longer fits. In one state after another, state banking laws have been critically reviewed by advisory groups, state supervisors, bankers' associations and state legislatures. In a significant number of states, completely new banking codes have been enacted, but even in the other states, major changes to existing codes have been adopted. Salaries and banking department budgets are significantly higher in almost every state, thereby assisting Governors in recruiting supervisors and the supervisors in recruiting examiners and other personnel of ability and breadth. Examiner training, particularly in newer types of credits, trust

department activities and automated record keeping, was intensified throughout the country.

As the pressure points within the direct control of state legislatures and state banking departments were relieved, attention turned inevitably to the Federal-level problems with which state banks and state supervisors had to contend on a recurring basis. The most dubious of the Comptroller's rulings were challenged by a number of state supervisors, and they won major victories in court establishing their standing to sue and vindicating the primacy of state branching laws incorporated by reference into the National Bank Act. A flagrant disparity in the state and local tax treatment of national and state banks was finally corrected by Congress last December after an adverse Supreme Court decision. Uniform call reports were adopted by the three Federal banking agencies and most of the states after years of effort. The Federal Reserve Board reversed itself on two rulings which had prevented state member banks, but not national banks, from having operations subsidiaries and loan production offices even when authorized by state law. Processing time for many applications was shortened by the Federal Reserve Board and the Federal Deposit Insurance Corporation through delegation of authority to regional offices and designated division heads on the central staff.

These developments, many of which resulted from your leadership, have all contributed to a noticeable improvement in the relative strength of state-chartered banking over the last six years. But a rough equality between state and Federally-chartered banking systems remains elusive in a number of major areas.

Basic parity still requires in the bank merger field a resolution of the divergent views of the Federal Reserve Board and the Comptroller of the Currency -- not merely on the weight to be assigned to different banking and competitive factors, but on the more basic questions of how existing competition should be measured and whether alternatives that are less anticompetitive must be considered at all. I consider it fortunate for the dual banking system that a number of bank merger cases are now on their way to the Supreme Court for definitive answers -- answers that presumably will be binding in the future on all three Federal bank agencies. The Federal Deposit Insurance Corporation has not been in the middle of this merger crossfire largely because of the size of banks involved in its decisions. But I can assure you we will be reexamining in the days ahead our general approach on these matters for purposes of the advisory opinions we render to the other bank agencies as well as for purposes of the mergers on which the FDIC itself must decide.

Basic parity also requires greater administrative efficiency in arriving at final decisions for state-chartered banks on a wide variety of applications and supervisory requirements. State banks generally have two regulators: their state banking department and either the Federal Reserve Board or the Federal Deposit Insurance Corporation. But more is involved in achieving an administrative efficiency equal to that of the Comptroller's Office than merely eliminating one of these two layers of supervision.

State banking departments, for example, tend to be catchalls for every type of financial regulation which a state legislature considers to be necessary in the public interest. Many of you are required by law to

supervise such diverse institutions as credit unions, small loan companies, retail instalment sales companies and pawnbrokers, in addition to mutual thrift institutions and commercial banks. State truth-in-lending laws and other consumer-oriented legislation may also be part of your responsibilities. Even with the best of staff, some of your time and energy will be devoted to each of these categories, and their myriad problems and requirements will stagger your examination force. By contrast, the Comptroller supervises only commercial banks. Most state supervisors, then, on the basis of statutory assignments alone, have a major administrative challenge right within their own departments -- a challenge which is compounded by the generally short terms they themselves serve. It is imperative that your Governors and legislators be continuously informed of the manpower and money you need to do all these jobs efficiently and well.

A second problem standing in the way of greater administrative efficiency at the state level is the nationwide scarcity of some of the specialized talent you need: instructors and programmers in automated data processing techniques used by banks, lawyers in state service who are knowledgeable in banking matters, and research economists able to give you and your legislature a realistic appraisal of credit needs, institutional performance and competition in local markets. I suspect the only practical answer for state banking departments here is a collective effort through this Association or in conjunction with the Federal agencies to develop a central corps of such people able to assist individual state departments at their request.

I do not minimize by any means the need for a simplification and reassignment of regulatory responsibilities between Federal and state agencies

as an important part of the solution to this problem of administrative efficiency for state-chartered banks. Such changes should, and undoubtedly will, be considered by the President's Commission on Financial Institutions -- just as they are now being studied in depth by a special committee of this Association. But getting even a majority consensus on one plan for revision and then putting it into effect will take time and effort. Our job in the interim, for both state and Federal supervisors, is to use the statutory authority and staff organizations we have now to make the present system work better. We should be striving cooperatively for results which achieve the benefits and speed of a single supervisor. As a former state superintendent, with a desire to restore a sense of purpose and experimentation to the state-chartered segment of the dual banking system, I would not expect or propose uniform national procedures to accomplish this. If we recognize each other's responsibilities and capabilities and if we proceed with goodwill and persistence, we should be able to meet our mutual requirements and still leave room for state-by-state variations.

It is to your credit that this Association, through its research programs, its guidelines for effective bank supervision, its evaluation project for measuring the performance of state banking departments, and its Special Committee to Restructure the Bank Regulatory System, is moving actively to capitalize on the progress of the last six years and to overcome the remaining obstacles to vigorous state banking systems.

It would be a fateful mistake, however, to assume that supervisory equality with the Comptroller's Office, once achieved, will guarantee the future of state-chartered banking. For like it or not, that future rests

ultimately with the Congress of the United States. And it is here that respect and confidence in state bank regulation is most needed.

Recent acts of Congress reveal unmistakably an impatience with state bank regulation, a lack of confidence in state supervision, and a readiness to grant new power and authority over state-chartered banks to the appropriate Federal agency. "Cease and desist" legislation, financial disclosure requirements, the Bank Protection Act, Federal truth-in-lending and the willingness to impose interest rate ceilings on noninsured state banks all reflect these sentiments. The original Bank Merger Act itself represented, at least in part, a Congressional judgment that the states were not doing an effective job of promoting or preserving bank competition.

It will not be easy to transform Congressional skepticism about state banking into understanding and active support, but I think four areas in particular should have your attention and leadership.

The first relates to the structure of financial competition within your individual states. This is the most sensitive of issues for every state supervisor, but passive acceptance of the status quo will gain neither Congressional respect nor Congressional confidence when we obviously are in a time of rapid technological, economic and competitive change. The instructions to your Federal Legislation Committee state as one of the basic principles of this Association that each state, and not the Federal Government, should determine the structure of financial competition within that state. The McFadden Act of 1928 agreed to this principle when it required national banks to follow state law in matters of branching and merging. But there is a more general national policy, enshrined in our antitrust laws, that business competition be encouraged and that restraints of trade that stifle competition be

discouraged. In its most recent amendments to the Bank Merger Act, Congress chose to emphasize this national policy by requiring that these antitrust criteria be considered first in any bank acquisition of another bank. Against this framework, I would ask whether the laws of your state promote or hinder competition among financial institutions. How frequently are they reexamined? Is the reexamination based on considered research and a desire to provide the people of your state with the best possible service at the least possible cost, or are the results dictated by the political clout of competing interest groups? On the administrative side, is the national interest in promoting competition among different types of financial institutions given sufficient consideration in your decisions as to public convenience and advantage on applications for charters, branches, and mergers?

The second area concerns one of the principal reasons for having a state-chartered banking system at all. Are the people of your state actually realizing the benefits of local innovation and experimentation based on state law and carried out by the wide variety of financial organizations that are state-chartered and state-regulated? At least in matters affecting banks and savings and loan associations, some observers believe that the states in recent years have only responded to innovations first thought out and adopted at the Federal level. Surely there is more that a decentralized dual banking system can offer the American people than a diffusion of regulatory power.

The third area involves the development of ways to finance the resolution of urgent community problems. In discussing the findings of a recent survey of American public opinion, Lou Harris reported that banks -- in this case, commercial banks -- had received high marks in extending the range and availability of bank services to more and more people, but had received very



unfavorable marks when it came to the role banks and bankers were playing in solving local community problems. I suspect the same could be said of bank regulators who have visible positions of leadership at both state and Federal levels. It would not surprise me to find that Congressional respect and confidence will be earned in direct proportion to the time, talent and leadership we give to the social problems in which they and the people generally are interested, as distinct from the narrower regulatory problems in which we traditionally have devoted our efforts. Are we putting as much time and thought as we should into such questions as how the required capital can be channeled into new housing, the rebuilding of our cities, and the revival of our mass transit systems? Are we, as supervisors, prepared to accept the fact that many investments now being made in these problem areas by concerned banks involve risks that cannot be accurately measured from either our past experience or theirs? Are we prepared to lead in matters of consumer protection or will we defer to others? To those who believe these problems are not the legitimate concern of bank supervisors, I would respond that times are changing, public expectations are changing, and so are concepts of effective bank regulation.

The fourth area is Congressional liaison and information. Congress is skeptical about state bank regulation in part because individual Members and committee staffs are frequently unaware of banking developments at the state level. Keep your state's Congressional delegation informed, through your own efforts or those of this Association, as to important changes in your state laws, the improvements you are making in your administrative capabilities as a regulator, the efforts you are making to insure better service at lowest cost to the people of your state, and the role you are

playing in the major community problems that are of concern to them. You can hardly hope to win Congressional respect and confidence without convincing Congress that state banking systems can be imaginative and responsive.

I would conclude by expressing my conviction that there is a continuing place in the American banking system for strong state banking systems that are close to the people and solicitous of their changing credit needs. It takes time, effort and imagination to make such a decentralized system work the way it should, but I am confident that with active supervisory leadership and with cooperation, respect and confidence in Washington, the dual banking system will be with us, vigorous and healthy, for many years to come.

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