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FDIC FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

Statement on

H. R. 8024, 94th Congress

A bill "To extend the authority for the flexible regulation of interest rates on deposits and share accounts in depository institutions, to impose a moratorium on the usage by financial institutions of electronic methods of funds transfers, and to improve public understanding of the role of depository institutions in home financing."

Presented to the

Subcommittee on Financial Institutions,
Supervision, Regulation and Insurance
Committee on Banking, Currency and Housing
House of Representatives

by

Frank Wille, Chairman
Federal Deposit Insurance Corporation

July 21, 1975

Mr. Chairman, I welcome the opportunity to appear before your Subcommittee today to present the views of the Federal Deposit Insurance Corporation with respect to H. R. 8024, 94th Congress, a bill "To extend the authority for the flexible regulation of interest rates on deposits and share accounts in depository institutions, to impose a moratorium on the usage by financial institutions of electronic methods of funds transfers, and to improve public understanding of the role of depository institutions in home financing."

Extension of Interest Rate Authority

Title I of the bill would extend for one year (until December 31, 1976) the statutory authority presently vested in the Board of Governors of the Federal Reserve System, the Board of Directors of the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board to regulate in a flexible manner the rates of interest or dividends payable by insured banks on time and savings deposits and by members of the Federal Home Loan Bank System on deposits, shares, or withdrawal accounts.

On a number of occasions recently the Corporation has gone on record as favoring the elimination of these Regulation Q-type interest rate ceilings on deposits as part of the Administation-proposed Financial Institutions Act (S. 1267, H. R. 5618 and H. R. 5619). While gradual elimination of these ceilings might be accomplished by administrative action, we believe that under present circumstances a total elimination of such restrictions could more appropriately be effected as an integral part of the Administration's proposed legislation. While we would urge prompt enactment of the Financial Institutions Act, we recognize that it is unlikely that the Congress will be prepared to act on the Administration's proposals prior to the present December 31, 1975 expiration date of the agencies' flexible statutory authority to limit deposit interest rates. In view of the probable disruption that could result from a termination of deposit interest rate ceilings on that date, we would support a one-year extension of this statutory authority as provided for in H. R. 8024.

Electronic Funds Transfer*

Title II of the bill would extend the life of the National Commission on Electronic Fund Transfers created by Pub. L. 93-495 so that the Commission's final report would be due within two years after Senate confirmation of the Commission's Chairperson, rather than two years after date of enactment (October 28, 1974) as the law presently provides. Title II would also impose a 90-day moratorium on the approval by any Federal agency regulating insured financial institutions with respect to the establishment or expansion of any system utilizing an electronic device for the purpose of authorizing the transfer of funds in a depository institution. Within the 90-day period, the National Commission would be required to review all existing EFT systems and all applications therefor on file with the financial regulatory agencies and to make recommendations for any further legislation needed to carry out the Commission's functions, including --

> "the Commission's proposal for monitoring all experimentation occurring with respect to all electronic fund transfer systems, the number and location of such experiments by class of financial institution, the Commission's method of evaluation including potential cost savings benefits to the public and the means to be employed by the Commission to insure a uniform system of experimentation." (§ 203)

Before broaching the substantive issues involved in Title II, I would like to call attention to one major technical deficiency in that Title as presently drafted. As noted above, the 90-day moratorium on EFT expansion, which would be imposed by § 202(b) of the bill, is phrased in terms of a prohibition against Federal agency approval of the establishment or expansion of EFT facilities by insured financial institutions. Insofar as such Federal agencies interpret existing law as not requiring their approval for the establishment of EFT facilities, as does the Comptroller of the Currency under current rulings, the 90-day moratorium as presently worded would not seem to have its intended effect. By way of further technical comment, it might also be pointed out that § 202(c)(2), (3), and (4) define terms which are not otherwise used in Title II.

*The Comptroller of the Currency, who serves as a member of the Corporation's Board of Directors, has submitted a separate statement of his views on Title II directly to the Subcommittee in his capacity as Comptroller of the Currency.

Title II is designed to give the recently authorized National Commission on Electronic Fund Transfers a brief opportunity to study this area and submit preliminary recommendations to the Congress before allowing insured financial institutions to proceed with the establishment and operation of such off-site EFT facilities without regard to Federal and State laws on branch banking. The threshold question for the three Federal bank regulatory agencies (Comptroller of the Currency, FDIC and Federal Reserve) is whether some or all such off-site facilities must be treated as "branches" under Federal banking law. The reason this question is so important is that if they are "branches" under Federal banking law, the three Federal bank regulatory agencies will then be legally bound by the provisions of State law governing the location and approval criteria for EFT facilities which banks headquartered in that State may wish to establish. If they are not "branches" under Federal banking law, the FDIC with respect to State non-member banks and the Federal Reserve with respect to State member banks would have only limited authority to supervise developments in this area unless some injury to the safety and soundness of individual institutions could be demonstrated. Presumably, notification requirements could be imposed on State-chartered banks which would allow the FDIC and the Federal Reserve to monitor the location, cost, operation and competitive impact of such facilities but advance approval or approval conditioned on certain changes in the planned operation of such facilities, e.g., in the terms of access to an inter-related network of such facilities, might not be possible. By contrast, the Comptroller of the Currency for national banks and State banking authorities for State-chartered banks would most likely have more comprehensive powers over the development of such facilities by virtue of their status as chartering authorities and primary supervisors for such banks. The Federal Home Loan Bank Board is not bound, as you know, by any similar provisions of Federal or State law in permitting federally insured savings and loan associations to establish branch or EFT facilities, since its governing statute is totally silent on the subject.

Of the many questions raised by EFT facilities, one appears to us to be relatively inconsequential, and that is whether a typical branch application and investigation should be necessary for these facilities even if they are to be considered "branches." We at the FDIC believe, and I am certain the other Federal supervisory agencies would respond similarly, that simpler forms and a different kind of review are desirable for EFT facilities than for manned, full-service branch facilities. That question is basically administrative, not legislative, and the four Federal agencies would undoubtedly adapt their present branch application procedures to the special needs of the new electronic environment.

On the merits of Title II of H. R. 8024, our view is that rather than imposing a moratorium on the expanded use of EFT equipment, which might prevent experimentation, technological refinement, and improved customer service, we would prefer that the Congress give the Federal bank regulatory agencies explicit legislative guidance on the "branch" issue and hence on the applicability of State law. If, however, the Congress should prefer to await the National Commission's report, or a judicial resolution of the "branch" question, before enacting legislation in this area and decides to pursue the moratorium approach, we believe that it would be inequitable to impose a complete moratorium on the development of EFT facilities by insured and regulated financial institutions when uninsured and unregulated firms in the private sector are not similarly constrained, e.g., nonbank credit card firms and major retailers.

Within many States, in ways fully consistent with State law, commercial banks and thrift institutions have already committed significant resources to the various types of EFT facilities, many of which are presently or nearly in place. In view of the significant policy issues to be dealt with by the National Commission, an analysis of the actual operations and continued competitive evolution of such facilities should serve as a valuable and necessary input to the Commission.

We believe, however, that the Subcommittee and the Congress could properly distinguish at the present time between the intrastate operation of such EFT facilities by insured financial institutions headquartered within that State and the possible interstate operation of such facilities by insured financial institutions. Most currently operated EFT facilities are in the former category, while possible interstate systems appear at this point in time to be only in various stages of early development. Few States have addressed themselves to this aspect of EFT development, and only a handful of banks or bank holding companies with "grandfather privileges" presently operate "retail" facilities or deposit-receiving branches outside their home States. On the other hand, the rulings of the Comptroller and the Federal Home Loan Bank Board may have the effect of giving federally chartered institutions a significant head start over their State-chartered competitors in the development of interstate EFT facilities which in due course the National Commission may recommend that the Congress limit or prohibit altogether. In this regard, these administrative rulings may result in a fundamental and basic change in the essentially local character of "retail" banking in the United States -- without benefit of any conscious study, analysis or approval by the Legislative Branch.

If, after review, the Congress were to decide that it did not wish to prohibit the interstate establishment and operation of EFT facilities altogether, there is a middle course which it might wish to consider. This would allow such interstate facilities only where the State of intended location has, by statute, explicitly authorized the establishment and operation of such facilities by an insured financial institution headquartered in another State. This would avoid the imposition of a Federal ban on interstate EFT activities that might well be permissible under explicit provisions of State law. Such State law provisions might, but need not, be limited to institutions headquartered in another State which had enacted reciprocal legislation authorizing insured financial institutions headquartered in the first State to establish similar facilities within its borders. Any remaining problems of competitive imbalance between State and federally chartered institutions headquartered in the same State could then be adjusted by changes in the State law in the headquarters State, just as they could be with respect to the intrastate facilities we recommend not be covered by a Federal moratorium.

The FDIC's position on Title II may thus be summarized as follows: We oppose the total moratorium on EFT facilities required by the present terms of the bill and would urge instead explicit Congressional guidance on whether or not such facilities constitute "branches" under present Federal law for purposes of applying the provisions of State law which might govern their location and approval. If this appears neither desirable nor feasible and the Congress believes <u>some</u> moratorium should be enacted while it awaits the report of the National Commission or a judicial determination of the "branch" question, we recommend that the moratorium not apply to the establishment of such facilities intrastate but only to the establishment of such EFT facilities across State lines (unless, possibly, such facilities are affirmatively authorized by explicit statute in the State of intended location).

Should the Subcommittee desire the Corporation's technical assistance in drafting the legislative provisions on which it may ultimately decide, we stand ready to help at any time.

Disclosure of Mortgage Loan and Deposit Data

Title III of H. R. 8024 would require all banks and thrift institutions located in standard metropolitan statistical areas to compile certain data relating to residential and commercial real estate loans and to time and savings deposits. In accordance with regulations to be issued by the Secretary of Housing and Urban Development, this information would be made available to the public for inspection and copying at each office of the institution. The loan and deposit data would be required to be classified according to the particular census tract where the real property is located or where the depositor resides. If the property or depositor is located outside a standard metropolitan statistical area, the classification would be by county. The provisions of Title III would not apply to loans made or deposits received prior to the date of enactment of the Title. Compliance with Title III's requirements would be enforced by the Federal financial regulatory agencies with respect to institutions within their direct jurisdiction, pursuant to their administrative enforcement authority under existing statutes.

While not so requiring, the bill would encourage real estate lending in certain geographic areas. In general, there is a legitimate question as to the extent, consistent with the protection of the bank's capital, that banks should be encouraged to make real estate loans in deteriorated neighborhoods. The blame for the degeneration of certain neighborhoods cannot be placed principally on the reluctance of financial institutions to invest in these neighborhoods. To do so is to ignore the realities of crime, poverty, delinquency, vandalism, and all the other social problems prevalent in today's world which cause declining market values. This is not meant in any way to condone discrimination based on race, color, religion, or national origin, but rather to emphasize that there are legitimate economic considerations which banks should be permitted to assess in the granting of real estate loans, particularly in declining neighborhoods.

The stated purpose of this legislation is to provide citizens and public officials with sufficient information to enable them to determine which depository institutions are fulfilling their obligations to serve the housing and business needs of the communities and neighborhoods in which they are located. It is far from certain, however, that the requirements of this Title would provide <u>sufficient</u> information to enable either citizens or public officials to adequately assess whether depository institutions are serving the needs of their communities. It would appear that, as a minimum, data relating to the demand for real estate loans in each neighborhood and data relating to rejected applications for real estate loans by neighborhood would be necessary to assess whether a depository institution is serving the needs of each neighborhood and the community.

While the information required by Title III is considered insufficient to fulfill its stated objectives, collection and recordkeeping of this information could be burdensome and time-consuming for many financial institutions. This would be particularly true for smaller banks which do not employ computer services.

There is one particular aspect of the recordkeeping requirements under Title III which appears unnecessarily burdensome to financial institutions. Under Section 304(a)(1), it appears that all information required to be compiled would have to be made available at each office of a depository institution. This would include detailed information regarding loans and deposits of the home office and all branch offices. The maintenance of a complete set of statistics at every office appears unnecessarily duplicative. It would appear more feasible for the home office to maintain a complete data file and each branch office to maintain only the information relative to its own operations or locality.

As a related matter, the FDIC in conjunction with the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Home Loan Bank Board undertook a Fair Housing Lending Practices Pilot Study in 18 standard metropolitan statistical areas throughout the United States for the period of June 1, 1974 through November 30, 1974. The purpose of the Pilot Study was to test the effectiveness of recordkeeping and reporting programs designed to enforce Title VIII of the Civil Rights Act of 1968. Three distinct data collection systems were utilized to determine which data were the most significant and which recordkeeping and reporting procedures were the most effective. One aspect of the Pilot Study related to the determination of whether the use of census tracts or the use of zip codes would prove to be more informative regarding property location and type and composition of neighborhoods.

Since Title III would place an extensive recordkeeping burden on many depository institutions, we would prefer that action on this legislation be delayed until the information it would require can be evaluated in the light of the results and conclusions from the Pilot Study conducted last year by the four financial agencies. The results of this Pilot Study for six of the 18 metropolitan areas were released early last May by the Federal Reserve and the FDIC, and the results for an additional six metropolitan areas were released by the Comptroller of the Currency on July 14. Results for the final six metropolitan areas should be released by the Federal Home Loan Bank Board in the near future.

If your Subcommittee should nevertheless decide to report favorably with respect to Title III, we would strongly recommd that, in addition to the amendment to § 304(a)(1) suggested above, Title III should be amended to confine its scope to <u>residential</u> mortgage lending and to delete therefrom all references to <u>commercial</u> real estate loans as well as to time deposits and savings accounts. The assumption that construction lending or other loans on commercial real estate should be confined to the localities where a financial institution's head office or a branch thereof is located is not valid in our opinion. Likewise, the assumption that financial institutions have a duty to make mortgage loans in a locality in direct correlation to the amount of savings and time deposits received from such locality seems also to be a questionable one. Lending institutions have an obligation to their depositors to exercise prudence and sound judgment in the investment of funds and cannot, consistent with this obligation, ignore factors affecting long-term values and loan security solely because of the amount or number of deposits received from a particular locality. In fact, if any such specific correlation between deposits and loans were to be required, the probable effect would be to afford a relative advantage to those institutions which make the least effort to provide savings facilities and other financial services convenient to customers residing in declining neighborhoods and, therefore, to discourage location of branches and similar facilities in such neighborhoods.