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Remarks of J. L. Robertson
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Federal Bank Supervision: The Real and the Ideal

A strong nation, like ours, is not afraid to confront its weaknesses. Hence, I regard it as a duty of public officials to speak openly about defects in our governmental structure, especially those for which they think they have solutions. Moreover, in my own case, at least, this is one way of expressing my appreciation for the opportunity to serve in a position of public trust.

Today I want to talk about defects in federal bank supervision. I might begin by telling you that when I think of it - as it exists today - I am reminded of a trick rider I saw, as a boy, at the Custer County Fair back in Broken Bow, Nebraska. He balanced on the backs of a pair of galloping horses - a foot on each one - with a great air of daring and unconcern. Of course, when I recall that scene in this context, the individual banker is in the position of the rider; he does not have any reins or other means of controlling the horses; he has three horses to ride, not two; each of them constantly threatens to gallop off in a different direction; and the rider is anything but unconcerned.

Everyone knows that federal bank supervision has grown up like Topsy, that it is divided among three agencies, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Reserve System, and that as a result there are overlapping powers and conflicting policies, along with inefficiencies and inconsistencies.

For many years this hodgepodge arrangement worked fairly well, but only because it was manned by people who understood that its successful operation required a high degree of comity and cooperation, together with an atmosphere of candor, patience, tolerance, and willingness to work harmoniously to solve the difficult problems that constantly arise.

However, dangerous weaknesses are built into the structure itself. This caused me to suggest, two years ago, that the federal bank supervisory powers now diffused among the three agencies should be transferred - lock, stock, and barrel - into a single new agency, a Federal Banking



Commission. It was my view that this would achieve needed uniformity and greater effectiveness and efficiency - as well as reduce the cost - of federal bank supervision.

One year ago, a Cabinet-level Committee on Financial Institutions, created by President Kennedy, reviewed, among other things, the practices of the federal bank supervisory agencies. The Committee noted, in its report, that the agencies had not always been able to achieve the needed cooperation and coordination. It recommended that stronger efforts be made to achieve harmony under common standards, regulations, and procedures. But its recommendation was a wary one, for it also suggested that reviews should be made from time to time to determine whether this approach was proving successful in anticipating and resolving major problems, and - if not, that consideration be given to a more basic solution, such as a consolidation of functions.

Those who, two years ago, or even one year ago, doubted the need for overhauling the federal government's bank supervisory machinery and hoped that the problems even then apparent could be solved through cooperation must now be convinced that their doubts were unwarranted and their hopes unfounded. Cooperation and coordination between the federal bank supervisory agencies have not improved; they have deteriorated markedly.

This is an unhappy fact for me to recount, for I have been a long-time devotee of the principle that cooperation and coordination can solve such problems among the federal agencies. But the facts brook no denial. Interpretations too contrasting to be rationalized have been promulgated concerning a number of banking powers and practices. I refer to conflicts resulting from such matters as a regulation purporting to authorize banks to underwrite revenue bonds in the face of a statutory prohibition; a ruling that "federal funds" transactions are not loans and therefore are not subject to statutory loan limitations; the question whether indebtedness represented by subordinated notes and debentures is part of a bank's "capital stock and surplus"; the intimation by one agency that national banks are not bound by the definition of the term "executive officer" in a loan regulation issued by another agency pursuant to authority vested

in it by Congress; the alleged availability of savings deposit privileges to business corporations; the proposal to duplicate supervisory authority over the international operations of national banks; and assertions regarding the lack of need for mandatory reserve requirements for banks that are members of the Federal Reserve System.

Just running through that abbreviated list calls to my mind the lines of Bobbie Burns, "Oh, wad some power the giftie gie us To see oursel's as 'ithers see us!" You will have to forgive me for rendering that quotation in the prairie accent of Broken Bow, Nebraska, rather than the burr of the Scottish Highlands, the land of my paternal ancestors. But perhaps bank supervisors collectively may need to ask a larger measure of forgiveness from bankers and the public for having gotten embroiled in such a hullabaloo of differences.

I do not propose to discuss these matters with you in detail today. Arguments over "Who said what, and why", tempting though they are, would impede our efforts to attain the real goal. I cite these differences only to demonstrate the imperative need to achieve coordination of supervisory effort at the federal level.

Any one of these conflicts, of course, would be bad enough. But the cumulative effect is what particularly bothers me. Bank supervision has been my business for thirty years, and I am deeply troubled by a situation in which different categories of banks are treated unequally under federal laws which were designed to apply equally to all. Moreover, I see this unequal treatment producing a serious state of confusion in the banks themselves.

To say that these conflicts impair federal bank supervision is to state the obvious. The evil goes much deeper than that. The result could be to create doubts about the integrity of all government agencies, and to diminish the confidence of the people of this country in our commercial banks. The recent letter from President Kelly of the American Bankers Association to the President of the United States underscores the existing confusion and unease in the banking community, and President Johnson's directive to

Secretary Dillon indicates the need and the will to do something about it.

The question before us is not just whether the regrettable breach among federal agencies can be patched up once again, and some measure of cooperation and coordination re-established. The basic question is, put bluntly: Can we continue to afford a supervisory system with the kind of built-in risks that this one has been demonstrated to have? The risk that three federal agencies will have irreconcilable, public differences of opinion, leaving commercial bankers up in the air, not knowing where they stand? The risk that one agency will fall under the domination of an individual who ignores or distorts statutes which he personally finds unacceptable? The risk that the several agencies will base their decisions - in merger cases, for example - on discordant interpretations of statutory standards, thus compelling banks to make their plans without the benefit of reliable guidelines by which to judge the worthwhileness of seeking supervisory approval? The risk of a "race of laxity" between competing federal supervisory agencies, each anxious to attract and retain banks in its own fold?

To state these questions is to answer them. It is obvious that we cannot continue to afford this "troika" system of federal bank supervision. Even if the current crisis were to subside, and the agencies were to return to their traditional hard-to-maintain harmony, the performances of the last two years are convincing proof that we must now take steps to avoid being vulnerable any longer to the risks and defects of this clumsy arrangement.

There can be no doubt in the mind of any reasonable man that action of some kind is essential. The problem is how to cut through the jungle of controversy and erect the essential framework of the kind of bank supervision that would best serve our needs.

Suppose we were to start afresh and endeavor to describe the ideal attributes of a federal bank supervisory structure. Is it possible that you and I here today, and

our colleagues elsewhere, could reach agreement on these characteristics? I think so. Let me list the attributes that come most strongly to my mind, and you can judge how closely they jibe with your own list.

I take it that we can all agree that the basic aim of bank supervision should be to promote a banking structure that is sound, attuned to community needs for banking services, adaptable to changing opportunities and technical advances, and competitive in the best sense of American economic enterprise. What are the characteristics of a federal supervisory structure that would be most likely to help in achieving these objectives?

First and foremost, the supervisor must be dedicated to the public interest. Conflicting detriments and benefits involved in decisions on charters, branches, or mergers, for example, should be resolved in favor of the public as a whole, even though this may result occasionally in a disappointed applicant. Over the long run, what is good for the country will prove to be good for the banking business.

Second, the supervisory agency should be objective in its judgments. Obviously, decisions of the agency should not be biased in favor of the industry, or any segment of it. Nor should they be biased against it, in the sense of trying to fit banking to some preconceived, Procrustean model. The decisions should be based on fact, reason, and informed judgment.

Third, is the need for it to be progressive in its outlook, and in the climate which it fosters within the industry. A positive commitment to progressive action and ideas is needed, for it is very easy for a regulatory authority to become complacent, to succumb to inertia, and not bother to respond to any but the conspicuously troublesome aspects of the industry. Ours is a dynamic economy, and it tends to generate ever-changing needs for banking services. Banks must respond to those needs, not only in order to serve the public interest but also to hold their own with competing institutions. The supervisor should be

alert to pioneering efforts within the industry - ready to adjust its regulatory attitude to accommodate resulting changes as soon as they are found to be sound and beneficial.

Pursuit of this objective, however, should not be carried so far as to undermine a fourth attribute of ideal supervision, namely, reasonable stability and consistency in decisions. If rigidity in supervisory posture is undesirable, so is vacillation. Changes in rulings and regulations ought to be promulgated with some sense of how long it takes the industry and its customers to adjust to changes in supervisory attitudes. What the industry and the public have a right to expect is that supervisory rulings will be well thought out, well integrated with one another, and with a probable duration long enough to make the expensive job of bank adjustment a paying proposition.

A fifth need, so obvious that it might easily be overlooked, is the need for basic fairness in the application of standards. Certainly every bank has a right to be treated on a par with the competing bank down the street. Special privilege has no place in the supervisory process.

The principle of fairness should also extend to the various types and classes of banks. It does not help the banking industry for one kind of federal regulatory status to confer discriminatory advantages, or to impose peculiar handicaps. Such differences distort competitive relationships, and may well lead to pussyfooting among the agencies. A far healthier banking structure can be attained if regulatory authorities aim for an equitable position for their banks, rather than a competitive edge.

Sixth, a necessary characteristic of any good supervisory authority is efficient, economical administration. I mean the good, old-fashioned virtue of getting the most for your money. Economy in government is an important attribute in a democracy, and the supervisory authority ought to set an example in the businesslike conduct of its affairs.

Seventh in my list of essential characteristics is the possession of sufficient authority for the effective

performance of supervisory responsibilities. I am not suggesting the need for any new, sweeping, or authoritarian powers, for I think that our present federal supervisory agencies hold among them all the regulatory power that is needed, if only it were employed in smoothly coordinated fashion. But the essence of bank supervision is the ability to supervise effectively, and there needs to be enough authority to make that possible.

An eighth requirement for a good supervisory authority is that its policy-making personnel should know the banking industry and know its problems. They should understand current banking practices and be aware of the operational consequences of the decisions they are reaching. And they should have enough intelligence and common sense to put their knowledge to constructive use.

Finally, just to be sure the ideal supervisory agency never acts out of ignorance or misinformation, I would add a ninth requirement - that it have wide-ranging and reliable channels of information. Bankers and their customers should be able to communicate their views to the agency promptly and directly. Furthermore, to the fullest extent practicable, these channels should be regular and public in nature, rather than secret. The regulated industry is entitled to be heard, subject to the discipline that what it says should be public knowledge. In that way, we can be best assured that legitimate grievances will be aired and private connivance avoided.

We have ended up with a list of nine attributes of an ideal federal bank supervisory agency. It is not complete. Upon reflection, each of us can think of others, but we have covered the main characteristics.

Agreeing upon supervisory objectives, however, is one thing and attaining them is another. As Woodrow Wilson reminded the framers of the Federal Reserve Act a half-century ago, financial reformers do not have a clean sheet of paper on which to execute their designs. We cannot reincarnate our system of financial supervision with a mere wish. Yet I am convinced we must reform it. It is admittedly defective. It has grown up haphazardly. Different

parts of it were created at different times, and not always with the other parts clearly in mind. Various appendages have been attached without enough regard to how they fit into the total system. As a result, we have a hodgepodge arrangement that no longer can be held together with the glue of good intentions alone.

Even though we must heed President Wilson's admonition, there is still a practical step that we can take to attain a bank supervisory set-up at the federal level that will possess the attributes we consider ideal and yet avoid the risks which make continuance of the present system intolerable. We can weld together the various parts of the system into a unified structure.

The need for more uniform and equitable regulation of banks clearly calls for consolidating the three federal supervisory establishments into one. The need for wisdom, stability, objectivity, and impartial consideration of various points of view argues against one-man rule and in favor of a supervisory board - a board whose members should be selected on a nonpartisan basis with the same care that is called for in the selection of judges for our highest courts. The need for technical competence and continuous focus on emerging banking problems, with their long-range supervisory implications, calls for a board with but a single job to do - rather than a combination of supervisory functions and others that are basically unrelated.

One ends up with a prescription for a supervisory structure very much like my suggested Federal Banking Commission, which is embodied in H. R. 5874, an exceptionally well-drafted bill that is pending in the House of Representatives. Its general terms, I hope, are so well known that it is unnecessary to dwell on them here. It provides for a single new federal supervisory agency - a five-man board solely responsible for all federal bank supervisory policies, actions, and decisions, with two administrative divisions handling bank examination and deposit insurance, respectively, whose actions would be subject to review by the whole Commission.



Looking back over the two years of comments and suggestions since the Federal Banking Commission idea was first broached, I am increasingly convinced that it represents a promising blend of the ideal and the pragmatic.

I hope you are convinced that a consolidation of federal bank supervisory functions in a single agency is a reasonable and good solution to a serious problem. But in any event, I urge you - individually and collectively - to express yourselves on the issue, to think it through and voice your conclusions. If the plan is good, say so, and say so loudly! If it is defective, point out the defects and suggest ways to correct them. The only course I decry is that of apathy, for this issue is too important to be decided by inertia.

You bankers are the people who are most directly affected by the defects in the current supervisory set-up and who would be most directly benefited by a shift to a better supervisory structure. You have not only a right but also a duty to speak out on the subject. The public is entitled to have the guidance of your informed judgment - and to have it now. A healthy and efficiently-regulated banking system is so vital to the economic well-being of the American people that we dare not temporize and thereby delay the adoption of a solution until after our banks have become bogged down in a morass of inequity and confusion.