

SENATOR MORGAN

Attached is a revised speech for the Pennsylvania Savings and Loan League.

Additional information:

- Pennsylvania is comprised primarily of mutual S&Ls, both Federal and State chartered, and with few, if any stock S&Ls.

- The group has been made aware of two insurance proposals. The first is a Magnuson bill to provide 100% insurance of public funds. The second is a St. Germain bill to provide \$300,000 coverage for IRA and Keogh plans.

SENATOR ROBERT MORGAN
SPEECH
PENNSYLVANIA SAVINGS LEAGUE, INC.
HERSHEY, PA.
JUNE 17, 1980 9:30 A.M.

PENNSYLVANIA - HOME OF INNOVATION

I know that you here in Pennsylvania are most familiar with the dramatic importance of savings and loans to the economic history of our country.

Pennsylvania is the home of financial institutions in the United States. The first commercial bank chartered in the U.S. was founded in Philadelphia by Robert Morris in 1781. In 1816, two mutual savings banks were founded, and Philadelphia was the home of one of them. The first savings and loan association was organized here in Pennsylvania in 1831 to meet the needs of industrial workers for home financing.

Pennsylvaniz has been the home for experimenatation and growth in depository institutions.

MY BACKGROUND & VIEWS ON GOVERNMENT REGULATION

Coming from rural North Carolina, a place of fierce independence and self-reliance, I have long been associated with the thrift industry. My first experience with financial institutions was on the board of a savings and loan. Since that time, I have spent many years as a State and Federal legislator and as a State Attorney General dealing with the problems and prospects facing your industry.

North Carolina, like Pennsylvania, is one of the original thirteen states, states which were responsible for throwing off the shackles of central government located in England. Both have a lasting commitment to the principle of government created by our revolution in 1776 and enshrined in our Constitution in 1789-- federalism. I know your interest in the principle of a dual system of government continues because just two weeks ago, I attended one of the finest seminars ever conducted by a university-- a symposium on federalism held at Temple University.

The reason I raise the issue of Federalism is to alert you to my support for the dual banking system which has grown up in our country as a result of our federal system. I have supported and will continue to work for the maintenance of the dual banking system. If for no other reasons than the need for alternatives and the maintenance of a plural society, I support this traditional approach to the regulation of depository institutions.

My support for the dual banking system will give you a key to my views on government regulation. The savings and loan industry is, by most estimates, the subject of the greatest government regulation in the private sector.

One reason for this is the fact that the housing industry, which the S&Ls support, represents not only an area of economic growth, but also a key element in our democratic system-- the tie of an individual to his home and his land. Homeowning gives the individual an economic and political stake in our system and by facilitating homeownership, S&Ls foster a stable political environment. Regulation has grown out of a sincere desire to protect this vital form of property ownership.

Regulation also grew out of several crises during the 1800's and the great Depression of the 1930's. Financial regulation arose from the Panic of 1873 and culminated in the Federal Reserve Act of 1913 and the Bank Act of 1933. Geographic regulation grew out of overextension of banks and speculation in the 1850's and was limited in the National Bank Act of 1864.

Recently, Congress has turned its attention towards deregulating the private sector. The airlines, trucking and oil companies have all been targets of deregulation. When the attention turned toward financial institutions, I was a bit apprehensive. Frankly, I have favored deregulation and I have supported cautious and careful actions by the Congress.

The Depository Institutions Deregulation and Monetary Control Act of 1980 did not fit that criteria to my mind.

Today, I want to touch briefly about items which relate to the role of government in the savings industry and about some actions proposed by the Deregulation Committee.

THE IMPORTANCE OF SAVINGS-- TAXATION

In comparison with other industrialized nations, our country provides no encouragements for the saver, and, through the tax laws, actually creates disincentives to savings. These disincentives have contributed to our lagging productivity and to our inflation rate.

The rate of savings as a percentage of disposable national income in 1976 was 4.8 percent. This past year, it temporarily dipped below 3.5 percent.

In England, the savings rate was 6.6 percent of income; in France, 13.1 percent; in Germany, 13.2 percent; in Switzerland, 17.2 percent; and in Japan, 25.3 percent.

With savings and investment at an all time low, the Congress has begun to take action. To encourage savings in the form of corporate stock ownership, the 1978 Revenue Act contained a provision lowering the effective capital gains rate. A drop in the corporate income tax created \$2 billion in additional funds for small businesses.

This past year, I sponsored a measure, along with Senator Lloyd Bentsen of Texas, to exempt from taxation the first \$1000 in savings interest and corporate dividends. As finally incorporated into the Windfall Profits Tax bill, an exemption was created for \$200 in interest for single taxpayers, \$400 for joint return filers.

While the \$200 is not a great incentive, it is a beginning. We have set the policy and indicated that the time has come to encourage savings through as many devices as possible. I am hopeful that in the months to come, we may increase the amount of interest exempted from taxation. I do not want to create a large budget deficit at a time of budget balancing, but increasing savings can only improve the economic situation that has demanded larger government spending in the past.

TAX WITHHOLDING

Now, however, at the very moment of the greatest need to encourage savings, the Treasury has revived a proposal made during the Ford Administration to withhold taxes on interest and dividends.

I worked against this proposal in 1976 and am doing so now.

Basically, the Treasury proposal calls for the quarterly withholding of 15% of interest income earned by a saver. The money would be transferred to the Treasury at that time.

Treasury estimates that the new withholding proposal will generate \$3.4 billion in revenues for the 1981 fiscal year. Of this amount, \$2.4 billion would result from accelerated collection of taxes normally paid in 1982 and \$1 billion would result from improved compliance with the tax laws.

This year, the desire for a balanced budget has increased the pressure for this withholding scheme. With spending ceilings set by the First Budget resolution, the demand has now been placed on all Senate Committees to cut spending and on the Finance Committee to raise revenues.

As I mentioned, I am opposed to the withholding plan. Let me explain why.

First of all, you need only make a cost-benefit analysis to see the waste of the plan. The U.S. League of Savings and Loans estimates that withholding would gross the Treasury \$230 million from S&Ls in the first year. The cost of compliance, with the expense of start up procedures, is estimated at \$573 million. After writing off this expense, the Treasury may only show a net gain in revenues of \$61 million.

There are other, more fundamental, objections. A paperwork nightmare may be created. Not only depository institutions would be engulfed in a sea of paper and computer time, but also the recipients of interest and dividend income would be losers. Exemption waivers would have to be created for certain individuals, additional filings and calculations would be required on individual income tax forms, and the lawyers and accountants would be the only winners.

Last, and certainly not least, the elderly and others on fixed incomes will be affected. The most constant savers are the elderly, and they will lose 15% of their income until they file for a refund a year later.

Withholding will discourage savings and would be a counterproductive move to much of what we are trying to do by balancing the budget. I am opposed to it.

SAVINGS AND THE DEREGULATION COMMITTEE--
MONEY MARKET CERTIFICATE DIFFERENTIAL

One of the major devices for savings and loans to attract funds have been money market certificates. On

these accounts, S&Ls have been able to offer a quarter-percentage-point greater interest than commercial banks.

The Deregulation Act, which Congress passed on March 31st, created a new Deregulation Committee to oversee the phasing out of interest ceilings, the utilization of NOW accounts by S&Ls, and other matters.

The newly created Committee has taken an action which complicates and makes unworkable the use of the differential and this could not have come at a poorer time.

A complicated formula has been set forth which contains a ceiling on the interest paid for 30 month certificates, but also contains a floor on certificate rates. IF the Treasury bill rate is 10.5%, ten commercial banks may pay no more than 10.25 percent, while thrifts may pay 10.5 percent. What happens when the Treasury bill rate drops below 9 percent is that the ceiling is maintained at 9.5 percent for thrifts and 9.25 for banks.

Even more complex are the rules for six month money certificates. When the Treasury bill rate is between $7\frac{1}{2}$ percent and $8\frac{1}{2}$ percent, the differential applies, while

above or below that rate the differential is dropped.

Only one week before the Deregulation Committee took these actions, Home Loan Bank Board Chairman Jay Janis warned the Senate Banking Committee that if mortgage rates were to fall, "...it is essential that thrifts keep the differential M(oney) M(arket) C(ertificate) rates are below 9 percent, at least for the rest of this year."

To my mind, the new rules go against Congressional intent, expressed explicitly in the Deregulation Act, which contemplated a gradual phase out of the differential and which specifically called for rate ceilings to be set at money market rates.

The ultimate effect of the Committee's action will be to keep interest rates artificially high.

I am disappointed in the actions of the Deregulation Committee and it is evident that close congressional oversight of its activities will be needed in the months to come. I look forward to close monitoring by the Financial Institutions Subcommittee of the Banking Committee.

SAVINGS AND THE DEREGULATION COMMITTEE--
BANK PREMIUMS

Another action of the Deregulation Committee raises concerns for savings institutions. On May 6, 1980, the Committee proposed a ban on premium promotions for all financial institutions.

The Committee was concerned about the violations of the \$5 and \$10 limits on premiums and the use of finders fees in large urban areas. The proposed rule would prohibit premiums given in relation to a deposit and would treat finders fees paid to third parties as interest and require that they be paid in cash.

Frankly, I feel a ban on premiums is a mistake. The Committee did agree to extend the time for comment on the rule, and I hope that you will take the opportunity to write Chairman Volcker expressing your concern.

At a time when we seek to encourage savings, the elimination of a competitive device such as premiums runs counter to the President's anti-inflation program and the spirit of the Deregulation Act.

One study has shown that among the choices available to S&Ls for raising funds-- advertising, premiums, or borrowing from the Fed-- the cheapest route is premiums.

While there are some problems with finders fees, the Deregulation Committee has adequate tools to address this problem directly. There is no need to throw out the baby with the bath water.

I have written to the Committee urging them to reconsider these proposed regulations with the following concepts in mind: the need to encourage savings, the desirability of continuing premiums while addressing specific abuses, and the impact of such a rule on the credibility of the Deregulation Committee.

I am optimistic that the Committee will not go ahead with the premium ban.

HOME MORTGAGE DISCLOSURE ACT

Another troublesome legislative matter of concern for the thrift industry is the proposed extension of the Home Mortgage Disclosure Act, better known as the HMDA. This law is due to expire on June 28th.

This law represents a continuing paperwork burden in a time of supposed deregulation. The information provided on these forms is not only an expense to the thrifts, it is also of little use to the public. We can protect the rights of individuals in better ways without adding to the cost of a home mortgage.

Indeed, some real deregulation might be attempted by exempting smaller institutions from reporting. Associations making less than 200 home loans a year, along with those with less than \$50 million in assets, hardly are big enough to affect neighborhood growth patterns.

Another idea for true deregulation might be the merger of the lending reporting programs contained in the Community Reinvestment Act, the Fair Housing Act, the Equal Credit Opportunity Act and the EMDA, into one comprehensive report with uniform regulations.

I would be interested in having your comments on such a proposal.

TAX EXEMPT REVENUE BONDS

A proposal has been made to allow unrestricted issues of tax-exempt mortgage revenue bonds for single-family housing; it is full of danger.

The House has approved legislation which restricts these bonds and calls for their elimination two years from now. The Senate Finance Committee, however, recently adopted a resolution calling for the unrestricted use of the bonds until December 31st. Consideration of this resolution by the Senate may be forthcoming shortly.

These bonds are a tremendous drain on the Federal Treasury. Because they are tax exempt, revenue losses will reach as much as \$1.6 billion in 1981 and as much as \$11 billion in 1984 unless restrictions are imposed.

The bonds weaken the fight against inflation, make budget balancing more difficult and injure the housing industry. The bonds crowd out other worthy municipal issues, such as public safety and services, and result in increased taxes.

State and local governments frustrate a national economic stabilization policy and drive housing prices even higher. Thus we have federal tax policy running counter to federal inflation policy. I hope that we can correct this in the near term.

THE OUTLOOK

Trouble spots remain for 1980, not only in the legislative arena but also in the marketplace.

The midwest, hit hard by automobile layoffs, and the Northeast, suffering from economic slowdowns, will continue to experience low demand for home financing.

There is no doubt that 1980 will be a year of decline for S&Ls. Mortgage lending will drop nearly \$40 billion and loan repayments will decline by \$9 billion from 1979 figures, \$12 billion from 1978 figures.

There is some optimistic news, too. With the drop in the prime rate and more savings being moved to longer term accounts, mortgage should become more available. This will be the foundation upon an economic recovery will be built.

The expectation among most experts is that improvement should come in the third quarter. Demand has been lagging in the 12 to 13 percent range, but the recent drop in California S&L rates to $12\frac{1}{4}$ percent may signal a move to the $11\frac{1}{2}$ percent range where thrift experts feel borrowing will renew with vigor.

1980 must be a year of reeducation and redetermination for S&Ls. The new laws which have created so many problems may also hold some opportunities and you must arm yourselves with the requisite skills to compete. The Deregulation Act contemplates a system of open market competition for the savings dollar, and the housing industry and many Americans are depending on your successful competition in that market.

We are opening the 1980's with a mixed picture. On one hand, there are problems facing the thrift industry. On the other hand, there are great opportunities.

Today, thrifts hold about 55 percent of all the home mortgages in the United States. During the 1980's, the demand for housing will rise to 22 million units, up from the 17.5 million of the 1970's. With changes in our living styles and with the baby boom, the number of households will rise from 67.5 million in 1970 to 97 million in 1980.

I believe that the challenge is there and I will continue my efforts to insure that the thrift industry has the tools to rise to the task.