BUILDING AND LOAN GUARANTEE FUNDS

HEARING

BEFORE THE

COMMITTEE ON FINANCE

UNITED STATES SENATE

EIGHTY-EIGHTH CONGRESS

SECOND SESSION

ON

H.R. 3297

AN ACT TO AMEND SECTION 501(c)(14) OF THE INTERNAL REVENUE CODE OF 1954 TO EXEMPT FROM INCOME TAXATION CERTAIN NONPROFIT CORPORATIONS AND ASSOCIATIONS ORGANIZED TO PROVIDE RESERVE FUNDS FOR DOMESTIC BUILDING AND LOAN ASSOCIATIONS, AND FOR OTHER PURPOSES

S. 739

JULY 21, 1964

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE

35-830 WASHINGTON : 1964

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WITNESSES

BUILDING AND LOAN GUARANTEE FUNDS

TUESDAY, JULY 21, 1964

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to notice, at 10:20 a.m., in room 2221, New Senate Office Building, Senator Harry Flood Byrd (chairman) presiding.

Present: Senators Byrd (presiding), Douglas, Gore, Talmadge, McCarthy, Ribicoff, Williams, Carlson, and Dirksen.

Also present: Elizabeth B. Springer, chief clerk.

The CHAIRMAN. The committee will come to order.

The committee today is considering H.R. 3297 to amend section 501 (c) (14) of the Internal Revenue Code of 1954, to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations. This bill is identical with S. 738 which was introduced on February 7, 1963, by Senator Daniel B. Brewster, of Maryland, for himself and Senator J. Glenn Beall, of Maryland. Also the hearing includes amendment 426 to H.R. 3297, introduced by Senator Jacob Javits, of New York, for himself and Senator Kenneth B. Keating, of New York, and Senator J. Glenn Beall, of Maryland. Amendment 426 would continue tax-exempt status to a State-chartered intstitution which is performing the same functions as the Federal Home Loan Bank System. I place in the record copies of the bill, the amendment, and departmental reports from the Treasury Department, and the Bureau of the Budget with attached letter by the Chairman of the Federal Home Loan Bank Board to the Director of the Budget.

(The documents referred to follow:)

[H.R. 3297, 88th Cong., 1st sess.]

AN ACT To amend section 501(c)(14) of the Internal Revenue Code of 1954 to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations, and for other purposes

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 501(c)(14) of the Internal Revenue Code of 1954 is amended by striking out "September 1, 1957" and inserting in lieu thereof "January 1, 1963".

SEC. 2. The amendment made by the first section of this Act shall apply only with respect to taxable years endings after the date of the enactment of this Act.

Passed the House of Representatives June 27, 1963.

Attest:

RALPH R. ROBERTS, *Clerk.*

[H.R. 3297, 88th Cong., 2d sess.]

AMENDMENTS Intended to be proposed by Mr. JAVITS (for himself, Mr. KEATING, and Mr. BEALL) to H.R. 3297, an Act to amend section 501(c)(14) of the Internal Revenue Code of 1954 to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations, and for other purposes, viz:

On page 1, line 8, insert "(a)" after "That".

On page 1, between lines 5 and 6, insert the following new subsection:

"(b) Such section 501(c)(14) is further amended by adding immediately after the semicolon the following: 'corporations or associations organized before July 22, 1932, and operated for mutual purposes and without profit performing functions substantially similar to those performed by Federal home loan banks;' ".

TREASURY DEPARTMENT,
Washington, July 21, 1964.

HON. HARRY F. BYRD,
Chairman, Committee on Finance,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the Treasury Department's views on amendment No. 426 to H.R. 3297 entitled "An act to amend section 501(c)(14) of the Internal Revenue Code of 1954 to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations, and for other purposes."

H.R. 3297 is designed to extend the exemption from income tax accorded by section 501(c)(14) to the Maryland Savings-Share Insurance Corp. In our report to you of September 25, 1963, we stated that, if your committee determines that the proposed extension of section 501(c)(14) is warranted, the Treasury Department would not interpose objections from a tax viewpoint. We expressed no opinion as to the merits of H.R. 3297 from the viewpoint of its effect on methods of insuring the stability of financial institutions.

The proposed amendment to H.R. 3297 is designed to extend to the New York State Savings & Loan Bank the exemption from income tax provided by section 501(c)(14). This would be accomplished by applying the exemption to "corporations or associations organized before July 22, 1932, and operated for mutual purposes and without profit, performing functions substantially similar to those performed by Federal home loan banks."

The factual background leading to the proposed amendment is set forth in a memorandum on amendment to H.R. 3297 regarding the New York State Savings & Loan Bank, appearing in the Congressional Record of February 25, 1964, at pages 3313 and 3314.

The Savings & Loan Bank of the State of New York was created by an act of the Legislature of the State of New York in 1914 and commenced operating in 1915 as the Land Bank of the State of New York. Its name was changed to the present one by the New York Legislature in 1932. The Savings & Loan Bank (hereinafter referred to as "bank") is organized without capital stock and membership is limited to savings and loan associations in New York. It is authorized to extend credit to, and act as a service bank for, its membership. The bank's function is to maintain a liquidity fund to make loans to associations which are short of liquid assets. The bank is also authorized to administer a fund for the insurance of savings accounts in savings and loan associations, but it does not perform this function.

Prior to 1952, savings and loan associations were exempt from Federal income tax. In 1935 the Internal Revenue Service ruled that the bank was also exempt from tax, under section 103(4) of the Revenue Act of 1932 and the corresponding provisions of prior law, as an integral part of the savings and loan system of the State of New York.

When the tax exemption of savings and loan associations was repealed by the Revenue Act of 1951, the predecessor of section 501(c)(14) was enacted to continue tax exemption for certain State-chartered organizations "operated for mutual purposes and without profit for the purpose of providing reserve funds for, *and insurance of, shares or deposits in*" savings and loan associations, cooperative banks, and mutual savings banks. [Emphasis supplied.]

The above provision was adopted by the conference committee and there appears to be no published explanation of the intended beneficiaries. However, the limited information in our files indicates that it was designed to continue the tax-exempt status of the Cooperative Central Bank and the Mutual Savings Central Fund in Massachusetts, the Savings Bank Guaranty Fund of Connecticut, and a similar organization in New Hampshire. The memorandum in support of the present amendment states in part that this 1951 legislation "was expected to cover the Savings & Loan Bank." However, we have no information indicating that the 1951 legislation was designed to include the bank. Moreover, with respect to the 1951 legislation the memorandum also states:

"The predecessor of section 501(c)(14) was added at the behest of the two mutual deposit guarantee funds in Massachusetts. *No thought was given to New York.*" [Emphasis supplied.]

It appears, therefore, that the proponents of the 1951 legislation either were unaware of, or were not concerned with, the situation of the bank, and that the similarities and dissimilarities between the bank and the other organizations exempt under section 501(c)(14) has not been considered by Congress. In any event, the bank was not then, and is not now, covered by the exemption because it does not provide insurance of shares or deposits in its member associations even though it does provide reserve funds for its members.

In 1952 the Internal Revenue Service received a letter, dated October 22, 1952, from counsel for the bank requesting a ruling that the bank was exempt under the predecessor of section 501(c)(14). This letter enclosed a legal brief in support of the ruling which set forth at length, in 18 pages, the powers and functions of the bank. This brief did not specifically allege that the bank in fact provided insurance for the shares of its members, but it did state in part:

"It would therefore seem certain that the statutory creation of the Savings & Loan Bank by the State of New York as a nonstock corporation *operated* for mutual purposes and without profit *for the purpose* of providing reserve funds for, and the *insurance of shares or deposits* in domestic building and loan associations in the State of New York, is the controlling factor in this case, and not subject to challenge." [Emphasis supplied.]

The legal brief did not raise, or make any issue of the fact that, the bank's failure to provide insurance for the shares of its members might be an impediment to a favorable ruling. The matter appears to have been routinely handled within the Service and a standard form ruling of exemption was issued under date of December 1, 1952. The only available administrative memorandum dealing with the case simply summarizes the ruling as one exempting the bank as one "* * * operated for mutual purposes and without profit for the purpose of providing reserve funds for domestic building and loan associations." There is no evidence available as to whether representatives of the bank were aware in 1952 of the significance of the fact that the bank did not provide insurance for shares, and it seems clear that representatives of the Service overlooked this point.

In September 1961 the bank requested the Service's advice as to whether the performance of certain additional functions by the bank would interfere with its tax-exempt status. The Service, in reviewing the information used as a basis for the 1952 ruling, discovered its prior error relating to the insurance of shares and notified the bank in December 1961 of the Service's intention to revoke its prior ruling.

Disposition of the matter was delayed during 1962 to permit the bank to pursue previously instituted efforts to obtain an amendment in the New York Legislature which would effectuate the bank's authority to provide insurance of shares. Although New York law authorizes the bank to administer a fund to insure the shares of members, such fund can be established by not less than 100 savings and loan associations whose share liabilities represent at least 33⅓ percent of the total share liabilities of New York savings and loan associations. The requirement of a minimum of 100 associations was adopted at a time when there existed approximately 350 New York associations. Apparently, the bank is unable to obtain the requisite 100 associations to establish an insurance fund to be administerd by the bank, since there are now only about 145 New York associations. The proposed modification of the New York banking law, which would have eliminated the requirement that 100 New York associations participate in the insurance fund, was not enacted. In July 1963, the Service revoked its prior ruling, effective for 1962 and subsequent years.

The proponents of the amendment contend that the bank should be entitled to exemption because it performs functions substantially similar to those performed by Federal home loan banks which are exempt from income taxes. They urge that the fact that the bank does not insure savings accounts should not be significant because, under the Federal system, this function is not performed by Federal home loan banks but rather by the Federal Savings and Loan Insurance Corporation. Of the 119 associations which are members of the bank, 106 are insured by the Federal Savings and Loan Insurance Corporation. If the bank were to provide insurance, such insurance would primarily be supplemental to Federal insurance.

From a tax viewpoint, the fact that the bank does not provide insurance of shares, but performs more limited functions than do other similar State-chartered reserve funds, would not appear to be a disadvantage. To the contrary, the Department's concern would be with the expansion of activities and sources of income eligible for tax exemption.

The Department is not in a position to express an informed opinion as to whether the bank does in fact perform functions substantially similar to a Federal home loan bank. There are certain resemblances between the two types of organizations. The principal functions of the two types of organization appear to be to provide additional liquidity and funds for seasonal mortgage lending to their members from resources consisting primarily of deposits of members and borrowing from the capital markets. The bank's statements of condition, earnings, and reserves and undivided profits for 1963 (copies of which are attached) show that the composition of its assets, liabilities, and sources of income resembles those of a home loan bank. However, the statement of earnings shows that $34,651.99 of total operating income of $600,449.98 was derived from a "mortgage service," which we understand is not a function presently performed by a home loan bank. The annual report of the bank for 1963 states that it provides a "complete mortgage accounting service, including escrow analysis and statistical reporting * * *. An off-line savings accounting program has also been developed and will be in use at the start of the second quarter of 1964. Equipment designed for a complete on-line system is presently on order and will be delivered during the third quarter of 1964."

We understand that home loan banks do not perform the above functions although the New York Home Loan Bank does provide a mechanized system for a punchcard reconcilement service for general drafts, Christmas club checks, dividend checks, money orders, and other accounts requiring the issuance of a large number of checks.

In view of the historical Federal income tax treatment of the bank, the Treasury Department would not interpose objections to this amendment to H.R. 3297 if your committee finds that the Savings & Loan Bank of the State of New York does perform functions substantially similar to those performed by Federal home loan banks, and if your committee determines that the proposed extension of section 501(c)(14) is warranted. The Department expresses no opinion as to the merits of the proposed amendment to H.R. 3297 from the viewpoint of its effect on the stability of financial institutions. On this latter issue, the Department defers to the views of the Federal Home Loan Bank Board.

The Bureau of the Budget has advised the Treasury Department that there is no objection from the standpoint of the administration's program to the presentation of this report.

Sincerely yours,

STANLEY S. SURREY, *Assistant Secretary.*

NEW YORK, N.Y., *January 17, 1964.*

ACCOUNTANTS' REPORT

The Board of Directors, Savings & Loan Bank of the State of New York:

We have examined the statement of condition of the Savings & Loan Bank of the State of New York as of December 31, 1963, and the related statements of earnings and reserves and undivided profits for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, based upon our examination, the accompanying statement of condition and statements of earnings and reserves and undivided profits, together

with the notes to financial statements, present fairly the financial position of the Savings & Loan Bank of the State of New York as of December 31, 1963, and the results of its operations for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

CALLAHAN & FRIES,
Certified Public Accountants.

Statement of condition, Dec. 31, 1963, with comparative figures at Dec. 31, 1962

	Dec. 31	
	1963	1962
Assets:		
Cash on hand and due from banks	$2,362,854.44	$1,773,416.35
U.S. Government securities	6,637,633.25	12,324,410.58
Loans to member associations	14,240,000.00	5,965,000.00
Accrued interest receivable	40,501.06	120,017.67
Other assets	21,571.00	24,183.04
Total	23,302,559.75	20,207,027.64
Liabilities:		
Membership shares	1,527,400.00	1,527,400.00
Deposits of member associations	14,512,232.28	18,230,749.25
Borrowed money	6,650,000.00	
Other liabilities	206,306.58	55,717.39
Reserves and undivided profits:		
Surplus	177,300.00	169,500.00
Reserve for bad debts	51,662.29	42,476.54
Undivided profits	177,658.36	181,184.46
Total	23,302,559.75	20,207,027.64

NOTE.—See accompanying notes to financial statements.

Statement of earnings, year ended Dec. 31, 1963, with comparative figures for the year 1962

	1963	1962
Income:		
Interest on loans	$250,374.81	$133,536.31
Interest on securities	310,454.82	354,003.25
Interest on certificates of deposit	45.14	32,590.28
Mortage service	34,651.99	24,093.00
Other income	4,923.22	4,372.37
Total income	600,449.98	548,595.21
Expenses:		
Salaries	95,952.18	66,434.92
Rent, light, and maintenance	17,735.25	15,812.28
Equipment rental	28,139.92	10,448.19
Interest paid:		
On members' time deposits	276,371.73	303,793.12
On borrowed money	44,210.10	
Other operating expenses	70,025.73	67,036.68
Total expenses	532,434.91	463,525.08
Net operating earnings	68,015.07	85,070.13
Net loss on sale of securities	14,520.48	749.73
Net earnings before U.S. income tax	53,494.59	84,320.40
Estimated U.S. income tax	1,850.00	
Net earnings	51,644.59	84,320.40
Application of net earnings:		
Transfers to—		
Surplus	7,800.00	7,700.00
Reserve for bad debts	9,185.75	42,476.54
Undivided profits	34,658.84	34,143.86
Total	51,644.59	84,320.40

NOTE.—See accompanying notes to financial statements.

Statement of reserves and undivided profits, year ended Dec. 31, 1963

	Surplus	Reserve for bad debts	Undivided profits
Balance at Dec. 31, 1962	$169,500.00	$42,476.54	$181,184.46
Add transfers from net earnings	7,800.00	9,185.75	34,658.84
Total	177,300.00	51,662.29	215,843.30
Deduct dividends paid			38,185.00
Balance at Dec. 31, 1963	177,300.00	51,662.29	177,658.30

NOTE.—See accompanying notes to financial statements.

Notes to financial statements, December 31, 1963

(1) U.S. Government securities are carried at cost less amortization of premiums. All of the U.S. Government securities and securities with a par value of $700,000 of a member association, with a short-term loan, are pledged to secure the borrowed money of $6,650,000.

(2) During the year 1963, a communication received from the U.S. Treasury Department stated that a review of the bank's exempt status as to Federal income tax disclosed that said exemption should not have been granted; that since the bank relied upon the exemption granted, the bank would not be required to file U.S. corporation income tax returns or be liable for Federal income taxes for years ended on or before December 31, 1961. A return was filed, as a cooperative bank, for the year 1962, and on that basis there was no tax.

Net earnings appropriated to general reserves and considered as a bad debt deduction in computing Federal income taxes for the years 1962 and 1963 amount to $67,162.29. If these appropriations are used for any purpose other than to absorb bad debt losses, the amounts so used will become taxable income in the year used.

(3) The Morgan Guaranty Trust Co. confirmed holding in trust custody account, $36,086,650 of securities held in safekeeping, free of any liens, for member associations.

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D.C., September 26, 1963.

Hon. HARRY F. BYRD,
Chairman, Committee on Finance,
U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your letter of June 20, 1963, requesting the views of the Bureau of the Budget on H.R. 3207, a bill to amend section 501(c)(14) of the Internal Revenue Code of 1954 to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations, and for other purposes.

The existing exemption applies to nonprofit mutual organizations which have no capital stock and were organized prior to September 1, 1957, to provide reserve funds for and insurance of shares or deposits in domestic building and loan associations, cooperative banks, and mutual savings banks. H.R. 3207 would extend the exemption by changing the cutoff date to include such organizations organized before January 1, 1963, with respect to taxable years ending after the date of enactment. The amendment is designed to exempt the Maryland Savings-Share Insurance Corp. which was created recently.

The Treasury Department in a report being sent to your committee, raises no objection to its enactment, on the basis of tax considerations. It observes that similar exemptions apply to comparable institutions in Massachusetts and Ohio and that it might be discriminatory tax treatment not to enact H.R. 3207. At the same time, Treasury points out that part of the justification for the exemption was eliminated by the Revenue Act of 1962, which levied taxes on the income of mutual savings institutions. Therefore, the Treasury would wish to reexamine its position should the bill be enacted and the exemption develop into a device for widespread tax-free accumulation of reserves.

Tax considerations alone, however, are not a sufficient basis for judging the merit of this proposal, as the letter of advice received from the Federal Home Loan Bank Board (copy attached) indicates. While the Maryland Savings-Share Insurance Corp. has objectives similar to those of the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation—as do the other State insurance organizations—and while the insurance provided by such organizations may be accepted by the public as roughly comparable to Federal insurance, they do not necessarily enforce comparable standards on the institutions which they insure. Favorable income tax treatment would tend to encourage formation of other State insurance corporations, with the attendant danger of competitive lowering of insurance standards from those established by the Federal Savings and Loan Insurance Corporation for the institutions insured by it.

Because of these and other considerations advanced by the Board, the Bureau of the Budget opposes the enactment of H.R. 3207.

Sincerely yours,

PHILLIP S. HUGHES,
Assistant Director for Legislative Reference.

Attachment.

FEDERAL HOME LOAN BANK BOARD,
Washington, D.C., July 16, 1963.

Hon. KERMIT GORDON,
Director, Bureau of the Budget,
Washington, D.C.

Attention of Mr. Phillip S. Hughes, Assistant Director, Legislative Reference.

DEAR MR. GORDON: Reference is made to legislative referral memorandum dated July 3, 1963, requesting the views of our agency on H.R. 3297 "to amend section 501(c)(14) of the Internal Revenue Code of 1954 to exempt from income taxation certain nonprofit corporations and associations organized to provide reserve funds for domestic building and loan associations, and for other purposes."

It appears that H.R. 3297 was passed by the House of Representatives on June 27, 1963, and is now pending before the Senate Committee on Finance.

Under present law, section 501(c)(14) of the Internal Revenue Code of 1954, as amended, an exemption from income tax is provided for nonprofit, mutual organizations which have no capital stock which are operated for the purpose of providing reserve funds for, and insurance of shares or deposits in, domestic building and loan associations, cooperative banks, or mutual savings banks. However, under said section of the Internal Revenue Code, the exemption from income tax applies only to organizations organized prior to September 1, 1957. H.R. 3297 would change the September 1, 1957, date to January 1, 1963, with the effect, as stated in the House committee report accompanying H.R. 3297, that the recently organized Maryland Savings-Share Insurance Corp. would be entitled to income tax exemption.

The Federal Home Loan Bank Board recognizes that the principal consideration as to the desirability of enactment of H.R. 3297 is its effect on the tax structure, and the tax consideration probably formed the basis for the Treasury Department's position on such bill as indicated in the following statement included in the House committee report (Rept. No. 459) accompanying H.R. 3297:

"The Treasury Department has indicated that it does not object to this bill although it stated that, if widespread use is made of these guarantee organizations to accumulate reserves, the basic exemption may merit reexamination in light of the revised taxation provided for these savings institutions by the Revenue Act of 1962."

However, it appears to the Federal Home Loan Bank Board that there is another factor which should be taken into consideration in determining whether H.R. 3297 should be enacted into law. Both the FDIC and the FSLIC were established by Congress to insure accounts in financial institutions. The objectives of the Maryland Savings-Share Insurance Corp., and other State-authorized account insurance programs are in large measure the same as the objectives of FDIC and FSLIC and this is essentially the ground stated in House Report No. 459 for the favorable report by the House Committee on Ways and Means.

Considering its responsibilities with respect to the Federal Savings and Loan Insurance Corporation, the Federal Home Loan Bank Board is of the opinion

that the interests of the United States are not served by a policy of bestowing tax exemption on various State-chartered insurance schemes for financial institutions, which frequently serve as substitutes for the more rigorous standards of Federal account insurance and may be accepted by the public as roughly comparable. They are not in fact equivalent. Although the capital stock of FSLIC has been retired, the United States has a financial interest in the FSLIC through the authorization in section 402(1) of the National Housing Act, as amended, for it to borrow from the Treasury up to $750 million outstanding at any one time.

In addition, the United States has an interest in the financial stability of FSLIC and institutions insured by it because of the relationship to the general economic health of the Nation. The enactment of H.R. 3297 may encourage the formation of other State-authorized insurance corporations which would reasonably expect similar income tax treatment and the Board does not favor encouragement of proliferation of such formations. This is said with recognition of the action taken in 1960 with respect to the Ohio Deposit Guarantee Fund. The following are the Board's reasons in support of the recommended policy:

1. Financial institutions have broad interdependence and failure of any State-authorized insurance fund may have adverse repercussions on FSLIC and institutions insured by it.

2. As a broad generality, savings and loan associations which are not insured by FSLIC represent the smaller and, in many instances, weaker classes of associations. Thus, they are not as well equipped to compete and are more apt to fail under economic stress than those insured by FSLIC. It would follow that the strain on State-authorized insurance funds, with less risk diversification, would be greater than in the case of FSLIC.

3. If the Maryland example becomes a pattern, the State-authorized insurance funds would be essentially privately operated without any real public control over the State-authorized insurance corporation. While the Maryland law (art. 27, sec. 161QQ) envisions an exchange of information concerning insured associations between the State supervisor and the Maryland Savings-Share Insurance Corp., no provision is made for independent examination of, or other control over, the insured associations by the State-authorized insurance corporation. The directorship of the corporation in Maryland will be largely composed of representatives of member insured associations. No provision is made in the Maryland statute for termination of insurance where an institution is pursuing an unsound course.

4. Because of disparities in face amount of insurance, State-authorized insurance programs for savings and loan associations might in future be established and used as competitive devices inconsistent with the objectives of insurance of accounts to promote stability. This possibility is present in Maryland in that the Maryland statute (art. 23, sec. 161SS) states that the insured limit "may not exceed by more than the sum of $10,000 the amount of prevailing insurance available from the FSLIC or its successor instrumentality from time to time."

For the reasons indicated, the Federal Home Loan Bank Board recommends against the enactment of H.R. 3297. It should also be noted that, in the opinion of the Federal Home Loan Bank Board, the Congress has a measure of control over the Nation's financial structure through its control of FDIC and FSLIC, which control would be subject to erosion if the effect of the enactment of H.R. 3297 would be to encourage other State-authorized insurance programs for financial institutions.

Sincerely yours,

JOSEPH P. MCMURRAY, *Chairman.*

The CHAIRMAN. In lieu of testifying in person, the Chairman of the Federal Home Loan Bank Board, the Honorable Joseph P. McMurray, has submitted a written statement giving the views of the Board on this legislation and the pending amendment.

(The statement of Chairman McMurray follows:)

STATEMENT ON H.R. 3297 BY JOSEPH P. MCMURRAY, CHAIRMAN, FEDERAL HOME LOAN BANK BOARD

Mr. Chairman and members of the committee, I have been asked to present the views of the Federal Home Loan Bank Board on H.R. 3297, which was passed by the House of Representatives and is now pending before your committee.

Under present law, section 501(c)(14) of the Internal Revenue Code of 1954, as amended, an exemption from Federal income tax is provided for nonprofit, mutual organizations which have no capital stock and are operated for the purpose of providing reserve funds for, and insurance of share or deposits in, domestic building and loan associations, cooperative banks, or mutual savings banks. However, under said section of the Internal Revenue Code, the exemption from income tax applies only to organizations organized prior to September 1, 1957. H.R. 3297 would change the September 1, 1957, date to January 1, 1963, with the effect, as stated in the House committee report accompanying H.R. 3297, that the recently organized Maryland Savings-Share Insurance Corp., would be entitled to income tax exemption.

The Federal Home Loan Bank Board recognizes that a major consideration as to whether H.R. 3297 should be enacted into law is its effect on the tax structure. The Federal Home Loan Bank Board expresses no view in that regard, but does believe that there is another factor which should be taken into consideration by the committee.

Both the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation were established by Congress to insure accounts in financial institutions. The objectives of the Maryland Savings-Share Insurance Corp., and other State-authorized account insurance programs, are in large measure the same as the objectives of FDIC and FSLIC and this is essentially the ground stated in House Report No. 459 for the favorable report by the House Committee on Ways and Means.

Considering its responsibilities with respect to the Federal Savings and Loan Insurance Corporation, the Federal Home Loan Bank Board is of the opinion that the interests of the United States are not served by a policy of bestowing tax exemption on various State-chartered insurance schemes for financial institutions, which frequently serve as substitutes for the more rigorous standards of Federal account insurance and may be accepted by the public as roughly comparable. They are not in fact equivalent. Although the capital stock of FSLIC has been retired, the United States has a financial interest in the FSLIC through the authorization in section 402(1) of the National Housing Act, as amended, for it to borrow from the Treasury up to $750 million outstanding at any one time.

The enactment of H.R. 3297 may encourage the formation of other State-authorized insurance corporations which would reasonably expect similar income tax treatment and the Board does not favor encouraging the proliferation of such corporations. The Board's reasons for this position may be summarized as follows:

First, financial institutions have broad interdependence and failure of any State-authorized insurance fund may have adverse repercussions on FSLIC and institutions insured by it. The United States has an interest in the financial stability of FSLIC and institutions insured by it because of their relationship to the general economic health of the Nation.

Second, as a broad generality, savings and loan associations which are not insured by FSLIC represent the smaller and, in many instances, weaker classes of associations. Thus, they are not as well equipped to compete and are more apt to fail under economic stress than those insured by FSLIC. It would follow that the strain on State-authorized insurance funds, with less risk diversification, would be greater than in the case of FSLIC.

Third, because of disparities in face amount of insurance, State-authorized insurance programs for savings and loan associations may be established and used as competitive devices in a manner inconsistent with the objective of insurance of accounts to promote stability. For example, the Maryland statute (art. 23, sec. 161SS) states that the insured limit "may not *exceed* by more than the sum of $10,000 the amount of prevailing insurance available from the FSLIC or its successor instrumentality from time to time." [Italic supplied.]

Accordingly, Maryland associations that are members of the Savings-Share Insurance Corp. could advertise accounts insured up to $20,000.

Fourth, a State-authorized insurance fund could be essentially privately operated without any real public control over it. For example, while the Maryland law envisions an exchange of information concerning insured associations between the State supervisor and the Maryland Savings-Share Insurance Corp., no provision is made in the statute for independent examination of, or other control over, the insured associations by the State-authorized insurance corporation. The directorship of the corporation in Maryland will be largely composed of representatives of member insured associations. No provision is made in the Maryland statute for termination of insurance where an institution is pursuing an unsound course.

In essence, the Board's objection to encouragement by the United States, through grant of Federal tax exemption, of proliferation of State-authorized insurance funds is that such State funds can reap the benefit of conditioning of the public to insurance of accounts in savings and loan associations by FSLIC, and thus gain public acceptance. At the same time, such State funds may not have the safeguards and diversification of risk of FSLIC. The likelihood of failure may be greater for such State funds than in the case of FSLIC, with possible adverse repercussions on FSLIC because of association in the public mind.

It is understood that your committee is also considering an amendment to H.R. 3297, which amendment is designed to extend to the New York State Savings & Loan Bank the exemption from income tax provided by section 501(c) (14) of the Internal Revenue Code. While the Federal Home Loan Bank Board has not had opportunity to study this matter at any length, my immediate impression is that the reasons assigned for recommending against extension of the tax exemption to State corporations engaged in insuring accounts are not as applicable to a State corporation designed to supplement the type of assistance provided savings and loan associations by Federal home loan banks.

It is understood that the Savings & Loan Bank of New York maintains a liquidity fund to make loans to New York savings and loan associations which are short of liquid assets. Broadly speaking, the same function is performed by Federal home loan banks for their members. An operation such as the Savings & Loan Bank of New York, so long as it is not regarded as a substitute for the Federal Home Loan Bank System, would simply represent a supplementary means of meeting liquidity needs of savings and loan associations. That the operation of the New York Savings & Loan Bank is supplemental to and not in substitution for the Federal Home Loan Bank System is borne out by the fact that nearly all of its members, it is understood, are also members of the Federal Home Loan Bank System. The Board, therefore, does not object to this amendment.

Advice has been received from the Bureau of the Budget that there is no objection, from the standpoint of the administration's program, to the submission of this report.

The CHAIRMAN. The committee is very much honored today to have the Governor and the two U.S. Senators from Maryland.

The Chair recognizes Senator Brewster.

STATEMENT OF HON. DANIEL B. BREWSTER, A U.S. SENATOR FROM THE STATE OF MARYLAND

Senator BREWSTER. Mr. Chairman and members of the committee, first of all, we would like to thank the chairman and the committee for giving us this chance to appear before the Senate Finance Committee on Senate bill 739, and House Resolution 3297. Senator Beall and I introduced the Senate bill early in the 1st session of the 88th Congress. The House bill was introduced on their side, and passed the House of Representatives on June 27 of last year.

The bills are identical, and are applicable only to the State of Maryland.

Briefly, the background in Maryland: In our savings and loan association industry in years gone by we have had some troubles. We have in the State met these and have carefully regulated our industry. It is now in excellent shape by virtue of legislation passed by our legislature and recommended by Governer Tawes.

One of the measures which passed the Legislature of Maryland was the creation of the Maryland Savings-Share Insurance Corp.

The bill before the Finance Committee today pertains to this corporation, a nonprofit State insurance corporation.

Rather than explain the details of the bill myself at this point, I would rather, with the chairman's permission, introduce the Governor of the State of Maryland, who has taken the lead in the regulation of this industry, has assured that it now has the confidence of the people of Maryland, and is here to testify on these two bills pertaining to the Maryland Savings-Share Insurance Corp.

Mr. Chairman, I present to you the Governor of the State of Maryland, Gov. J. Millard Tawes.

STATEMENT OF HON. J. MILLARD TAWES, GOVERNOR OF THE STATE OF MARYLAND

Mr. TAWES. Thank you, Senator Brewster.

Mr. Chairman, and members of the committee——

The CHAIRMAN. Governor Tawes, we are honored to hear you.

Mr. TAWES. I take the unusual step of appearing before you today to urge a favorable report by this committee of H.R. 3297 because the financial strength of Maryland Savings-Share Insurance Corp. is an important commitment of my administration as Governor of Maryland.

As you perhaps are aware, in 1960 Maryland was the object of a raid by outside interests who sought to exploit the then unregulated State building and loan business.

The lack of regulation prior to this time simply reflected the soundness of that business as conducted by Marylanders. In short, no regulation has been necessary. I do not recollect the name of any Maryland building and loan that failed during the great depression, but I do know that the number was infinitesimally small.

In any event, the appearance in Maryland building and loan circles of identfiably corrupt elements became apparent during the February 1960 legislative session. A bill was drafted and passed, but my experience as comptroller of Maryland for 17 years and bank commissioner for 3 years told me that this bill, with all the hasty amendments attached thereto, was not an effective regulatory measure.

On April 6, 1960, I vetoed the bill, and on May 1 of that year I appointed a commission composed of leaders in the building and loan field, representing both Federal and State associations, and leading legislators. Under the experienced and able chairmanship of Richard W. Case, this group prepared a comprehensive and sound regulatory measure. This was introduced in the 1961 legislative session, and despite strong opposition, it was enacted into law.

When its opponents petitioned this act to referendum—which would have delayed its effect until after the 1962 general election—I convened a special session of the legislature on June 9, 1961, at which a similar, emergency act was passed.

Nevertheless, I knew that the problems which we faced could not be solved by regulation alone. I realized that the unscrupulous operators, whose Ponzi-like promotions were then beginning to collapse, would considerably damage the previously splendid reputation which the Maryland savings and loan business had enjoyed in the eyes of the public.

So, initiating the second phase of my program for dealing with the financial fires which these operators had started, I appointed a second commission, under the chairmanship of the late Col. John S. Shriver, the then director of Maryland's Fiscal Research Bureau. This commission was charged with the duty of recommending a sound, viable, industry-sponsored system of insurance for free share accounts held by the public in State-chartered building and loan associations.

I did not then and I do not now believe that the building and loan business must come under the control of the Federal Home Loan Bank Board in order to be conducted on a sound basis. The history of State-chartered associations in Maryland during the depression is the most vivid evidence to which I can point in support of my feeling.

The result of the Shriver Commission's work was the creation of Maryland Savings-Share Insurance Corp. by special act of the 1962 Maryland General Assembly. This corporation has already made giant strides toward its goal—to restore public confidence not only in State-chartered associations but in the entire building and loan business throughout the State of Maryland.

Maryland Savings-Share Insurance Corp. does not depend upon governmental subsidies or grants to maintain its existence. No public funds of any kind are involved. The credit of the State of Maryland cannot be pledged by the corporation. To the contrary, every capital dollar of the corporation has been contributed by its members. In short, Maryland Savings-Share Insurance Corp. is a singular example of people helping themselves, for their mutual benefit, and for the benefit of the members of the general public as well.

In order to attain full strength and to fulfill its purpose, this corporation needs and deserves, freedom from taxation. John Shriver recognized this when the corporation's legislative charter was being prepared. That charter contains a complete exemption from State taxation.

The calculated and deliberate dishonesty of a relatively few people operating in the Maryland building and loan field has caused me more distress during my administration than I can possibly convey to you at this hearing, and I have given my best efforts not just to stop the excesses but to effect reforms which will at once strengthen the building and loan business and prevent any future upheaval in this field.

One aspect of this program is sound and reasonable regulation. The other is a State-sponsored, industry-supported program of mutual insurance. The future economic health and welfare of the latter program is before you gentlemen today.

I am trying to speak as impersonally as I can, although the vilification to which I have been subjected as a result of the financial crisis of the past few years makes it difficult.

But what I want to convey to the committee is, first, my complete confidence in this corporation and, second, my unshakable conviction that the defeat of H.R. 3297 will be a serious blow not just to those

who have toiled with me in these matters but to the whole saving public in Maryland, without bringing any identifiable benefit either to that saving public or to the Federal Government.

Gentlemen, I thank you very much for this opportunity to present this statement to you.

The CHAIRMAN. Thank you, Governor. We are very much pleased to hear from you.

Senator Beall?

STATEMENT OF HON. J. GLENN BEALL, A U.S. SENATOR FROM THE STATE OF MARYLAND

Senator BEALL. Thank you, Mr. Chairman, and members of the committee. I am grateful to the committee for providing me with this opportunity to testify in support of H.R. 3297.

This House bill is identical to a bill introduced by Senator Brewster and myself in the Senate.

It will amend section 501(c)(14) of the 1954 Internal Revenue Code so as to exempt from Federal income tax the Maryland Savings-Share Insurance Corp. This corporation is a nonprofit, quasi-governmental agency chartered by the Maryland Legislature to insure deposits in State-chartered savings and loan associations.

As the committee members are aware, similar exemptions apply to comparable institutions in Massachusetts and Ohio. In Maryland the savings and loan industry has recently weathered trying times. I am gratified that my own efforts back in 1958 resulted in the cleaning out of unscrupulous promoters who were taking advantage of savings and loan investors in Maryland. Not only did I take the Senate floor and warn the public about doing business with these unscrupulous operators, but as a member at that time of the Senate Banking and Currency Committee I instigated a committee investigation and hearings.

Following the exposé the State legislators, and officials took up the cause, and today the Maryland savings and loan associations are free of these unscrupulous operators.

Speedy approval of this legislation will end the job we started in the Senate back in the Banking and Currency Committee in 1958, and enactment of this legislation will culminate our efforts to insure that investors in our Maryland savings and loan institutions will never again experience those dark days of 1958.

Thank you, Mr. Chairman, and members of the committee.

The CHAIRMAN. Thank you very much, Senator Beall.

The Chair recognizes Senator Brewster to introduce Mr. Case——

Senator BREWSTER. Thank you, Mr. Chairman.

The CHAIRMAN (continuing). As the next witness.

Senator BREWSTER. Mr. Chairman, and members of the committee, with us today are the members of the board of directors of the Maryland Savings-Share Insurance Corp., and also Mr. Borden, the president of Loyola Federal Savings & Loan Association, the largest savings and loan association in Maryland, also a federally insured association. He is here to support this measure.

The president and chairman of the Maryland Savings-Share Insurance Corp. is a well-known Maryland attorney who is beside me, Mr. Richard W. Case. I would like to present Mr. Case to the committee. He will testify to the details of the measure which Senator Beall, the Governor, and I support.

Mr. Case.

The CHAIRMAN. Mr. Case, proceed, sir.

STATEMENT OF RICHARD W. CASE, CHAIRMAN OF THE BOARD OF MARYLAND SAVINGS-SHARE INSURANCE CORP.; ACCOMPANIED BY CHARLES E. ORTH, CHAIRMAN OF THE BOARD, BUILDING SAVINGS & LOAN COMMISSIONERS OF STATE OF MARYLAND; AND C. EDWARD KLINE, PRESIDENT, CITIZENS BUILDING & LOAN ASSOCIATION OF SILVER SPRING, MD.

Mr. CASE. Mr. Chairman, and members of the committee, at the outset, I should like to say that I have a somewhat detailed and perhaps technical prepared statement which is being circulated and which I wish to have introduced here, but with the committee's permission, rather than read that statement I would prefer to summarize what is said there and perhaps touch upon some other matter which are not completely included in the statement.

Additionally, we have here today copies of the first financial statement of the Maryland Savings-Share Insurance Corp., together with its bylaws, rules, and regulations, and these also I should like to have considered, or ask they be considered by the committee in its deliberations.

(The bylaws and regulations were made a part of the committee files.)

Now, the specific object of the subject legislation here today is to amend the Internal Revenue Code, section 501(c)(14) by advancing the date when certain nonprofit corporations established to insure the deposits of savings and loan associations may qualify for exemption from Federal income tax.

The bill now provides that such associations created on or before September 1, 1957, qualify for this exemption. The subject bill would advance that date to January 1, 1963.

There is only one association or corporation which now gains the benefit, we are told, from the provisions of section 501(c)(14), and that is the Ohio Guarantee Fund.

The Maryland Savings-Share Insurance Corp. would, if this bill becomes law, be put in the same position as the Ohio fund, and gain exactly the same tax benefits that that fund now receives.

With reference to the background, Mr. Chairman, and members of the committee, of this legislation, it would be presumptuous for me to elaborate on the remarks of Governor Tawes. I would say, however, that the committee should keep in mind the framework in which this legislation came to Maryland, and that was that the situation in the savings and loan field had reached dire results. We had, before the storm was over, over 30 associations put into court receivership or conservatorship or under court protection at one time or another, and

these associations amounted to more than $40 million in savings of the people of Maryland.

Additionally, there were very unfortunate malefactors who were convicted, some of them very prominent people, two of them former members of the House of Representatives, one of them the speaker of the House of Delegates of the State of Maryland.

Now, within this framework, Governor Tawes sponsored a two-pronged attack. He realized, first, that adequate regulation was needed to govern the savings and loan industry in the future, to set the guidelines for the workaday situations that developed in that industry.

But he also recognized that there was a cardinal element lacking in regulation, and that was the restoration of public confidence in the savings and loan business, and it was to the second point that the Maryland Savings-Share Insurance Corp. was directed, because it was felt that if a State-sponsored program of insurance could be implemented by law, that the people of Maryland would regain the lost confidence that they had lost in the savings and loan business.

So the act was passed by the general assembly.

Very briefly, as has already been stated, it establishes a nonprofit nonstock corporation. All of the funds of this corporation come from capital contributions made by the members of the corporation. Having no stock, of course, the corporation has members, and these members pay a one-shot capital contribution equal to 2 percent of the free share accounts of each association.

The corporation today, as the financial statements before the committee will show, has in the bank in excess of $2,450,000 in securities, as a result of these capital contributions.

Now, a salient provision of the law, Mr. Chairman, and members of the committee, is that there can be no distribution of profits of any kind to anybody in the Maryland Savings-Share Insurance Corp. group.

Senator WILLIAMS. What would happen if there were a liquidation of this corporation?

Mr. CASE. If there was a complete liquidation, Senator, it would be very difficult to say. It is possible to argue that this money would escheat, the profits would escheat to the State because the law clearly says that there shall be no distribution of profits of any kind to any member, and I would suppose that the answer is either as I have suggested, or if the corporation were liquidated by legislative act, the legislature would have to make provision for this, and, of course, it could do this.

Senator WILLIAMS. There is nothing in the bylaws, then, that would spell out that it would not go back to the banks, is there?

Mr. CASE. The law itself says that, sir, and therefore it was felt not necessary to put it into the bylaws of the corporation. The actual, the legislative directive makes that point very, very clear.

Now, this corporation, Mr. Chairman, and members of the committee, is, in fact, a quasi-State agency. There are at least seven reasons why I make this statement, and they are briefly as follows:

First, the bylaws, rules, and regulations of the Maryland Savings-Share Insurance Corp. must be filed with the appropriate State agencies before they became effective.

Second, any amendment in these rules, regulations, or bylaws must first be approved by the appropriate State agencies before they can become effective.

Third, every member association of the Maryland Savings-Share Insurance Corp. must be examined by a State examiner who must certify that it is ready for membership in the corporation before it can become a member of the corporation.

Fourth, the Governor appoints 3 members of the 11-man board who are public members and represent the public on the board of directors of the corporation.

Next, all supervisory letters or status letters of any kind sent by the director of the Maryland Department of Building Savings & Loan Associations is forwarded to the Maryland Savings-Share Insurance Corp. for its consideration.

Sixth, the files of the Maryland department are made available to the Maryland Savings-Share Insurance Corp. with references to any member.

And, lastly, the corporation has been permitted to use a very attractive seal which we call a symbol, which resembles, as I think the members of the committee will recognize, the great seal of Maryland, by an official opinion of the attorney general.

Now, the relationship, fiscalwise, with the State, is as Governor Tawes has stated in his prepared statement.

First of all, the corporation is free from all taxes in the State of Maryland; and, secondly, the legislation expressly states that the credit of the State cannot be pledged for any of the obligations of the corporation.

The law has many other detailed provisions, and I don't intend to take the committee's time to go into them.

I would like to say, however, that one provision controls the investments that can be made limiting these investments to very narrow and safe type of medium.

This corporation began its operations in late May of 1962. I was appointed chairman of the interim board of Governor Tawes, and I met with 11 dedicated people. These men, Mr. Chairman, and members of the committee, worked around the clock, virtually around the clock, to get guide rules that could be used to solicit membership, and guide rules were prepared in a sufficient status to solicit membership in June, 3 weeks after the corporation had met.

It is a surprising and, I think, heartwarming thing to know that during the first week solicitation more than 58 associations involving more than $118 million in free shares, had asked to become members of this corporation, and they hadn't even seen the bylaws, rules, and regulations that they were going to be governed by, a most remarkable performance.

I shall not try to outline the rules and regulations which are before you, Mr. Chairman, and members of the committee, but suffice it to say that the whole bent of these documents is to insure that the member associations conduct safe and sound operations.

I would like to point out that if a member association does not, in the opinion of the board of directors of the insurance company, or is not conducting a safe and sound operation, it can be expelled from membership, and if it is expelled from membership, either it must

notify its depositors or the insurance company will notify the depositors for it.

It has been suggested that the high standards prevailing in the rules and regulations add a second, and perhaps more stringent regulatory agency in the State of Maryland over the member associations.

Now, Mr. Chairman, there is a great public benefit to be gained, it seems to me, by the passage of this act, and I should like to say just for a minute what I think the theoretical benefit is, which I hope is obvious, and, secondly, give you an actual example of what has happened already in the State of Maryland to show how the people of our State benefit from the existence of this insurance company.

As a theoretical thing, of course, the protection of the peoples savings is the business of government everywhere, and the Maryland Savings-Share Insurance Corp. reaches an area which the Federal Savings and Loan Insurance Corporation does not reach.

This subject insurance company covers the small association, the well-run, well-managed old line association. But these associations in most part are too small to qualify for FSLIC coverage, and, therefore, they are denied that coverage.

This corporation gives the savers coverage, and therefore, it supplies a very needed useful public purpose, in my judgment.

As a practical matter, let me cite one case which might be of interest to the members of the committee.

Last year, just about world's series time, as a matter of fact, I was taking the day or so off. I was called at my home and said that one of our assured associations had been the unfortunate victim of a theft. This was embezzlement, and, of course, nobody can guard against this. This association had been strenuously examined by State examiners, it had a surplus in excess of 10 percent, its mortgage portfolio was extremely sound. The insurance company granted the insurance.

About 6 months later we found out that an employee of that association had been stealing from it for over 6 years, and she had gotten away with about $65,000. The association was insolvent, and there was nothing to do but put it under court protection.

In the old days this would have meant a very disastrous Christmas for some of Senator Beall's constituents, but the Maryland Savings-Share Insurance Association was able to step into the breach, supplied legal and accounting talent in this particular case, and before Christmas every depositor except two who were not officers and directors of this association had been paid in full in cash the amount of their savings share accounts. The two who were not paid, one had an account over the limit, which I might say is $20,000, and the other we didn't know about, because the defaulted employee had just failed to put this depositor's name on the books.

When we found out who it was we petitioned the court for authority to pay this individual, too.

Now, I cite this merely as an example of the public good that this company has done in Maryland and will do in the future.

I don't intend to take the committee's time to go into a great many statistical comparisons between insured associations covered by the Maryland Insurance Co. and those covered by FSLIC. Suffice it to say that gaged on every yardstick with which I am generally familiar, the Maryland insured associations are stronger than those covered by

FSLIC. Based on the ratio of reserves to potential liability, this is so.

Now, if the committee please, it seems to me then that there are three essential reasons for giving favorable report on this subject legislation.

The first reason which I would suggest is, and one which I have not touched on, is that this matter has been thoroughly investigated by the Treasury Department, not once, but twice. The favorable report which accompanies the report of the House Ways and Means Committee is the second time this matter went into—has been gone into by the Treasury Department, the first time being when a similar bill was introduced by Senator Brewster when he was in the House of Representatives in the 87th Congress. The Treasury at that time went into the matter. We filed briefs with them, they were completely satisfied, as they were on the subject legislation.

Secondly, it seems to me that it would be a gross, almost incomprehensible discrimination against the people of the State of Maryland were this legislation not enacted, because the indentical purpose is being served now by the Ohio Guarantee Fund in Ohio. As a matter of fact, the Ohio fund served in many ways as a pattern for the Maryland Savings-Share Insurance Corp.

We had many conferences with the executive vice president of the Ohio fund. Our bylaws to some extent are drawn from their fund.

The CHAIRMAN. May I interrupt you a moment? Was special legislation passed to give Ohio tax free status?

Mr. CASE. Yes, sir; it was. That was the 86th Congress, in Public Law 86-428, in the 86th Congress.

The CHAIRMAN. Is that the only State that is tax free?

Mr. CASE. Yes, sir; I understand this is true.

The history of this legislation is rather interesting on that score, Senator Byrd. In 1951, as you know, the Congress amended the Internal Revenue Code to withdraw the tax free status of all savings and loan associations. At that time, however, this particular section, section 501(c)(14) was passed to continue the tax free status of two Massachusetts organizations, one in Connecticut, and one in New Hampshire. It is my understanding, and the Treasury Department's report confirms this, that these corporations are no longer in the business of insuring the deposits of savings and loan associations.

In 1960 the bill was, or this section, was amended to provide that it should cover all associations created on or before September 1, 1957, and the express purpose of that act was to grant this Ohio fund tax exemption, exactly why we are here today, sir.

Senator WILLIAMS. Is the faith and credit of the State of Ohio pledged in any manner?

Mr. CASE. No, sir; it is not.

The CHAIRMAN. How many States have operations such as you mentioned?

Mr. CASE. Senator, to my knowledge, Maryland and Ohio are the only ones, although I believe New York is seeking to have this but have not yet done it.

When we say operations, I am referring in a very limited sense to the insuring of free share accounts in domestic savings and loan associations.

Senator GORE. Mr. Chairman, I would like to suggest that the witness has just made a very significant suggestion to the committee, that is, that other States are considering doing this same thing. In my opinion, if you open up this tax loophole permitting associations to hide away reserves with tax exemption, then we will not have just New York but perhaps all of the States coming in, and this may seriously weaken the Federal Savings and Loan Insurance Corporation, and the regulatory activities of that corporation in the public interest.

Senator WILLIAMS. There is another point that disturbs me; and that is, the use of the State seal and the State name which implies to the depositors that these loans are insured with the faith and credit of the State in back of it when in reality all the State is lending is its name. The assets of the corporation, to insure these deposits are very small in relation to the amount of insurance involved. It is not exactly solvent. One failure of one major institution and you are bankrupt, and yet you are giving the impression you are insuring all desposits up to $20,000, not $10,000 as under the FDIC, the Federal Corporation, the faith and credit of the United States is put in back of this to guarantee the payment.

If the States put their faith and credit to some extent back of this insurance and guarantee these deposits I would support your bill. I can see giving the implication to the depositors that the State of Maryland or the State of Ohio or whatever State may be involved is guaranteeing these deposits may fool a lot of depositors.

As I see it, the depositors may well be putting their money in these banks thinking they have a guarantee by a State when in reality all the State is giving is the use of its name.

I am quite concerned about this.

Mr. CASE. Senator, there are several answers to that. First, I should like to answer the statement that was made immediately preceding yours, if I may, and that is that this is not a scheme to hide away the reserves of member associations. These associations contribute their capital knowing full well that they will never get any benefit. As a matter of fact, they are getting rather a serious loss since they are not able to earn on the moneys that are put up into the capital deposit and will never get any income from that.

Senator WILLIAMS. Do they charge it off as business deduction?

Mr. CASE. No, sir.

Senator WILLIAMS. The contibutions to this fund?

Mr. CASE. No, sir. This is a capital contribution. It is not subject to deduction.

Senator WILLIAMS. You mean the individual savings and loan cannot charge it off?

Mr. CASE. No, sir. The only privilege they have is to show the asset as an asset on their books.

Senator WILLIAMS. Well, if they carry it as an asset on their books then there must be some indication that it would be recovered in the case of liquidation.

Mr. CASE. Well, I must say——

Senator WILLIAMS. Otherwise, it is a false claim as an asset.

Mr. CASE. It is an asset. I am sure they do. I don't represent any savings and loan, myself, sir, but I think——

Senator WILLIAMS. You follow what I am getting at?

Mr. CASE. But it is probably carried as an asset on their books.

Senator WILLIAMS. If it is carried as an asset there must be in intention to recover the money in the event of a liquidation, otherwise it is a false asset.

Mr. CASE. Accountingwise you may have a good point there, Senator, but in my judgment there will never by any return of income of any kind.

Senator WILLIAMS. That is beside the point.

Savings and loans are not allowed to carry as an asset something which they will never be able to recover, that is irrevocably gone; are they? I wish you would clarify that for the record.

Mr. CASE. Would the Senator permit me to consult some of my associates here?

Senator WILLIAMS. And furnish it for the record if you wish.

Mr. CASE. Yes.

It has been suggested that perhaps the reason this is done, Senator Williams, is that the withdrawing—an association can withdraw from this insurance company.

Senator WILLIAMS. That gets back to what I said; they would withdraw their assets.

Mr. CASE. You said if the whole thing dissolves, what happens? If they withdraw on a piecemeal basis, then they would get back only the amount they contributed, and this over a period of time, this is also true in Ohio.

Do I make myself clear on that?

Senator WILLIAMS. Suppose there is a major failure in the State of Maryland, a failure which would go beyond the assets of the corporation. Could any of the members start withdrawing their contributions prior to it?

Mr. CASE. No, sir. They cannot withdraw under the rules within a period of 12 months, and then can only be given a certificate of participating interest. But I think the point that you made, Senator, with reference to the failure of one big association, if I could meet that I would like to do so. Under the rules and regulations, all of the associations who are members of this corporation are in a sense pooled, and they, the associations, have agreed by becoming members that they will stand for a call on their assets to any amount that is necessary on a pro rata basis. So that if an association did fold up, heaven forbid, but if it did, then the corporation has a total of upward of $150 million of assets to call on before the whole thing would collapse. In other words, Senator, I should like to have you understand, sir, that this is a mutual organization with this corporation sort of as the focal point. It has a certain amount of money in the till now, which I might say amounts to considerably more to the insured liability than the Federal Savings and Loan Insurance Corporation has to its potential liability.

But this is only the first reserve against which losses can be charged, and if there is a further loss which would exhaust that $2,500,000, which is the amount that we have now, then, of course, additional calls can be made.

Senator WILLIAMS. Are they irrevocably bound to pay that assessment under any circumstance?

Mr. CASE. Yes, sir, The bylaws provide, sir, that they shall constitute an irrevocable contract between the association and the Maryland Savings-Share Insurance Corp., and that by applying for membership this is in substance an offer to contract, which when the membership is accepted is an acceptance of that offer and that these liabilities can be enforced in court.

I was saying, Mr. Chairman, and members of the committee, that in my judgment it could be, and I hope it will be in yours, a rank discrimination to give the people of Ohio this legislation, and not give it those of us in Maryland who have fought so hard with Governor Tawes to remedy the situation that we had there in 1960–61 period.

The third reason which I urge as a basis for the support of this legislation is, of course, the public benefit and welfare. I have already talked about that.

I think that this corporation is doing a very good job. It is a second line of defense against any types of fraud and other things that can happen in fiscal institutions.

It does carry out the program of a sovereign State, it does protect savings in those associations where FSLIC does not reach, and it is, as Governor Tawes suggested, an example of a mutual effort of the people of a sovereign State to help themselves through mutual action.

I, therefore, would ask you to give a favorable consideration, sir, to this legislation.

In closing, I should like to say that there is here in the hearing room today with me Mr. Sam W. Borden, who is president of Loyola Federal Savings & Loan Association, a savings and loan association having assets upward of $160 million to $170 million. It is either the first or second largest savings and loan association in Maryland, and one of the largest in the United States. It is federally insured.

Mr. Borden is here as an advocate of this legislation, and if the committee would care to hear a statement from Mr. Borden, he would be glad to give it.

The CHAIRMAN. Mr. Case, how much is involved in the way of taxation?

Mr. CASE. Senator Byrd, of course, thinking in terms of the Federal situation, it is infinitesimal. It is expected that this corporation will have approximately $2½ million in investable funds. If you multiply $2½ by 4 percent, you come up with $00,000 of income. Assuming that it is going to take us about $35,000 or $40,000 to run it, so you would get down to maybe $45,000 and it would be whatever—it would not be quite 50 percent, but it would be a 48-percent break, that is what it is.

But the reason that the tax exemption is needed is that the way that this corporation will build up its reserves is to keep putting this money into additional securities, and every year the situation gets stronger and stronger as time goes on. But actually the tax effect or impact is minutia.

Senator WILLIAMS. What will the tax liability be for the last fiscal year or last calendar year, assuming this bill is not passed?

Mr. CASE. In the last fiscal year it would have been nothing, Senator Williams, because the corporation had just been organized, and the running expenses were in excess of income.

During the first 6 months, first 5 months, of calendar year 1964 the corporation had net income after the payment of expenses of about $10,600.

Now, I am at the pleasure of the committee as to whether or not Mr. Borden should be heard. I will say that he sponsors and favors this bill and, perhaps, that might be sufficient.

(The prepared statement of Mr. Case follows:)

STATEMENT OF RICHARD W. CASE, CHAIRMAN OF THE BOARD OF MARYLAND SAVINGS-SHARE INSURANCE CORP.

PURPOSE

Mr. Chairman and members of the Senate Finance Committee, the purpose of H.R. 3297 is to amend section 501(c)(14) of the Internal Revenue Code of 1954 which exempts from income taxation certain nonprofit corporations organized to provide insurance for free share accounts of domestic savings and loan associations.

Under present law, an exemption from income tax is provided for nonprofit, mutual organizations having no capital stock which are operated for the purpose of providing insurance for shares or deposits in domestic savings and loan associations if such organizations were created before September 1, 1957. The subject bill (H.R. 3297) would extend the income tax exemption now available to qualifying organizations to similar corporations created before January 1, 1963.

The original exemption was added to the Internal Revenue Code by the Revenue Act of 1951. It was enacted to continue the tax-free status of the Cooperative Central Bank and the Mutual Savings Central Fund in Massachusetts, the Savings Banks Deposit Guarantee Fund of Connecticut, and similar organizations in New Hampshire. In 1960, by Public Law 86–428, 86th Congress, H.R. 6155, the exemption was enlarged to provide tax-free status for the Ohio Deposit Guarantee Fund (the Ohio Fund), a mutual deposit guarantee association organized in December 1956.

It is our understanding that the Ohio Fund is the only organization now benefiting from the provisions of Internal Revenue Code section 501(c)(14).

The Maryland Savings-Share Insurance Corp. (MSSIC) was created by an act of the General Assembly of Maryland to accomplish the same purposes as those of the Ohio Fund. The two organizations ar identical in their overall framework and objectives. MSSIC was organized in November 1962. Accordingly, the object of H.R. 3297 is to extend to MSSIC the same income tax treatment as that now enjoyed by its counterpart in Ohio, i.e., the Ohio Fund.

BACKGROUND

Prior to 1960, there was no regulation of any kind over Maryland domestic savings and loan associations, the free shares of which were not insured by the Federal Savings and Loan Insurance Corporation. In that year, however, certain members of the General Assembly of Maryland became concerned over the fact that the savings and loan industry had become the pawn of dubious operators who were largely of non-Maryland origin. To correct this situation, a bill was introduced into and passed by the general assembly for the purpose of instilling a degree of regulation for the industry.

Although acceptable in design, the 1960 act was fraught with inconsistencies and abounded with obvious loopholes. To meet this situation, Gov. J. Millard Tawes vetoed the bill and appointed a nonpaid, nonpolitical commission to devise a workable and acceptable regulatory act.

The commission organized in June 1960. It was composed of legislators, industry leaders, and one person (its chairman) having no connection with the savings and loan business. The capacity of this commission is testified to by the fact that one of its members is now a judge of the U.S. District Court for the District of Maryland, one is a member of the Supreme Bench of Baltimore City, one is a judge of the municipal court of Baltimore City and one is the former U.S. district attorney for Maryland and currently the Democratic candidate for the U.S. Senate.

The investigation and research conducted by the commission revealed that the fears concerning the Maryland savings and loan industry were not unfounded. Meeting on an average of twice weekly, the commission devised a realistic and workable bill to cope with the situation. This bill was subsequently introduced into the General Assembly of Maryland, and, after one of the most bitter legislative battles ever witnessed in Annapolis, become law.

Opponents of the new regulatory act were quick to respond with countermeasures. During the early spring of 1961, they were successful in obtaining sufficient signatures on a referendum petition to suspend the operation of the act until the fall of 1962. The reaction of the State administration to this move was quick and sure. A special session of the general assembly was called, and an emergency measure was passed which adopted all of the salient features of the suspended act. The constitutionality of the emergency law was tested in the courts and was upheld by a decision of the Maryland Court of Appeals.

That the Maryland savings and loan situation was badly in need of correction is clearly evident from the sequence of events that followed the passage of the regulatory act. Over 30 Maryland savings and loan associations involving more than $40 million in free share accounts were placed under court protection. Convictions for mail fraud and larceny after trust were numerous. The malefactors included not only out-of-State fiscal opportunists, one of whom was a Member of the U.S. House of Representatives, but also a Maryland congressman, a member of the Maryland House of Delegates and the speaker of the Maryland House of Delegates.

The executive commission which devised the Maryland regulatory act believed that simple regulation of the savings and loan industry would not be sufficient to restore public confidence to the business. For this reason, ways and means were sought to regenerate lost public esteem. The idea most acceptable to the commission was the creation of a sound insurance program that would protect the depositors in Maryland institutions that were not covered by the Federal Savings and Loan Insurance Corporation.

Because time did not permit a thorough investigation of a program of insurance by the commission, it recommended that the Governor appoint a second group to inquire into the feasibility of such a plan. In making this recommendation, particular emphasis was given to the Ohio fund which was then in operation and which enjoyed an exemption from Federal income taxation.

Responding to this recommendation, Governor Tawes, in June of 1961, created a second executive commission which was charged to inquire into and report upon the possibility of establishing a nonprofit organization, similar to the Ohio fund, which would have as its object insuring of free share accounts of State-chartered, uninsured savings and loan associations.

The second executive commission organized immediately and undertook its assignment. In this connection, numerous meetings were held with the executive vice president of the Ohio fund. By January 1, 1962, the second commission had completed its studies and thereafter recommended the passage of an act to create a nonprofit organization, patterned after the Ohio law, which would have as its object the insuring of free share accounts in Maryland savings and loan associations. This act was passed by the General Assembly of Maryland during its regular session in 1962.

MARYLAND SAVINGS-SHARE INSURANCE CORP.

Maryland Savings-Share Insurance Corp. was created by chapter 131 of the acts of the General Assembly of Maryland of 1962 (the act). It is a nonstock, nonprofit corporation, vested with powers, privileges and immunities of other corporations, the purposes of which are "to promote the elasticity and flexibility of the resources of member associations, to provide for the liquidity of such associations through a central reserve fund, and to insure the free share accounts of such associations." The act specifically provides that the earnings of the corporation shall be accumulated by it "and no part thereof shall be returned to the member associations."

The membership of the corporation is limited by law to those associations, the financial affairs, solvency, management and directorship of which have been certified as eligible by the director of the Maryland Department of Building, Savings & Loan Associations. Thus, there exists an absolute legal liaison between MSSIC and the Maryland authorities who are charged with the responsibility of regulating the savings and loan industry in that State.

Other salient provisions of the act are as follows:

1. *Controlled investments.*—The act limits the power of the corporation to invest its funds to the following: cash, insured bank or savings and loan deposits, interest-bearing municipal or corporate bonds, corporate stocks (within defined limits), Maryland ground rents and mortgages upon unencumbered real property purchased from a member association.

2. *State control.*—The appropriate State authorities exercise a continuing control over the affairs of MSSIC. The Governor is required to appoint 3 of the 11 authorized directors. No association may become a member until it has first been certified for membership by the director of the Maryland Department of Building, Savings & Loan Associations. The bylaws, rules and regulations of the corporation must be filed with the Maryland Department of Assessment and Taxation, and any change or modification thereof must have first been approved by appropriate State agencies.

3. *State fiscal responsibility.*—MSSIC is financed entirely from capital contributions made by its members. The act specifically provides that under no circumstances shall the faith or credit of the State be pledged for the purposes of the corporation.

4. *Insurance limits.*—The act empowers the corporation to insure free share accounts in member associations but limits the amount of this insurance to a sum not in excess of $10,000 above the amount of prevailing insurance available from the Federal Savings and Loan Insurance Corporation from time to time.

The act provided that the Governor of Maryland should appoint an interim board of directors of 11 people to prepare workable rules and regulations for the corporation. It further provided that applications for membership could be received by the interim board, that such applications should be reviewed by the State department of building, savings and loan associations, and that the corporation should cease to exist if it did not accept for membership at least 25 associations having free share accounts of $25 million which had filed applications for membership prior to August 1, 1962.

In May 1962, the Governor appointed the interim board of directors of MSSIC. Meeting weekly for the purpose of setting overall policy and the development of an outline of governing rules, this board was in a position to solicit applications for membership in the corporation by the end of the first week in June. In making this solicitation, prospective members were told only that if accepted, they would be required to pay a capital contribution equal to 2 percent of their free share accounts.

By June 11, applications for membership had been received from 58 associations having approximately $90 million in free share accounts. One week later, these figures had increased, respectively, to 105 associations and $118 million. The most remarkable aspect of these events is the fact that the associations applied for membership on faith alone—they had not received a copy of any bylaws, rules, or regulations at the time they applied for membership.

The organization of the corporation was completed on November 23, 1962. At that time, 140 associations having free share accounts of $108 million were approved for membership by the board.

As of May 1, 1964, Maryland Savings-Share Insurance Corp. had 164 members with total assets of $144,873,348. Of this number, 133 associations were incorporated between the years 1869 and 1938, and 84 associations were incorporated before 1915. These statistics provide ample evidence of the fact that the member associations are truly old-line, conservative institutions that have weathered the storms of countless depressions and periods of economic adversity without a faltering step.

BYLAWS, RULES, AND REGULATIONS

The bylaws, rules, and regulations of MSSIC create a contractual relationship between the corporation and its members. They set the standard of conduct and responsibility to which each member association must adhere if its insurance is to continue in force. The bylaws, rules, and regulations are the product of countless days of study, drafting, discussion, and debate. They are tailored to fit the precise conditions which confront MSSIC and its members and draw, where appropriate, upon the rules and regulations of the Ohio fund and the Federal Home Loan Bank Board.

Prominent among the provisions of the rules and regulations of MSSIC are the following:

1. Applicants for membership are required to submit complete data not only as to their charters and bylaws but as to the occupations and experience of all officers and directors and as to their fiscal affairs during at least the previous 3 years.

2. Each application is preliminarily reviewed by the corporation's membership committee and is then referred to the director of the State department of building, savings and loan associations. This State officer must then examine the applicant's affairs and certify that they are in order, after which the membership committee makes a final report.

3. Before any applicant is admitted to membership, its application must receive a favorable vote of the majority of the whole board of directors.

4. Applicants and members must agree to amend their charters or bylaws in order to insure conformity not only with laws of Maryland but with the bylaws of MSSIC.

5. Applicants and members must agree to provide any fiscal reports and statistical information which the MSSIC board may at any time require.

6. Member associations must also agree that, should the State department notify MSSIC that the member is violating certain provisions of State law, then MSSIC may appoint a person to serve on the board of directors of the association.

7. No member is permitted to make any representations about its membership in MSSIC except to display the advertising symbol and to state that its accounts are insured up to $20,000 by MSSIC, a corporation created by the laws of Maryland.

8. Members must maintain a loss reserve of not less than 6 percent of the aggregate withdrawal value of their free share accounts. If an applicant does not maintain this minimum reserve, it must execute and deliver to MSSIC a hypothecation of accounts in amount sufficient to meet this minimum.

9. Any member which does not maintain general reserves and undivided profits equal to 10 percent of the aggregate withdrawal value of its free share accounts must maintain a net liquidity fund equal to 6 percent of its total free share accounts.

10. Members must keep MSSIC advised of delinquent accounts and of any change in dividend rates.

11. Any capital change in a member association by way of consolidation, merger, dissolution, or transfer of property must be submitted to MSSIC for prior approval by its board of directors.

12. Members must comply with any recommendation made by the membership committee of MSSIC, must maintain fidelity bonds in amounts equivalent to the requirements of the Federal Home Loan Bank Board, and must generally conduct their affairs in a safe and sound manner.

If a member association is violating any provision of the laws of Maryland, conducting an unsafe or unsound business, or is found to be in violation of any of the corporation's bylaws, rules, or regulations, it may be expelled from membership. In the event that a member is expelled, it must notify its free share holders of this fact, and failure to give such notice will authorize the corporation to supply the deficiency.

PUBLIC BENEFIT

That the investing public is the prime beneficiary of MSSIC is a self-evident fact. Member savings and loan associations in Maryland are not only subject to the Maryland regulatory act but are also required to meet and maintain the higher standards imposed by the corporation's bylaws, rules, and regulations. Failure to comply with these higher standards may cause a member's explusion from MSSIC, and notice of this fact must be made known to all of its free share holders. The investor is thus assured of a continuing surveillance over his savings.

It is an unfortunate fact, however, that all fiscal institutions are exposed to the possibility of loss through the defalcation or fraud of dishonest employees. No regulation can prevent this; no insurance program can prevent it. But an insurance program can, in such cases, obviate the attendant hardships which befall the innocent investor when an employee of a savings institution has breached his sacred trust.

MSSIC has already demonstrated its public value in this area. In late October 1963, it was discovered that an employee of an old-line savings and

loan association in Cumberland, Md., had appropriated to her own use in excess of $50,000 of the association's funds. This defalcation rendered the association insolvent.

The insolvent association was insured by MSSIC. At the time of its original examination, the insolvent association had shown an excellent financial picture; its mortgage portfolio was sound; it had reserves in excess of 10 percent of free share capital; its board of directors was composed of leading business and professional people in the Cumberland area; and its president was a long-time member of the Maryland bar.

Within 3 days after the theft was reported publicly, the executive committee of MSSIC had met and devised a program to eliminate the attendant hardships which would have befallen the association's depositors had MSSIC not been in existence. At its own cost, MSSIC supplied accounting and legal services to the circuit court of Allegany County which had assumed jurisdiction over the association. Before Christmas, every depositor who was not an officer or director of the insolvent association (except two) had received in cash the full amount of his deposit. Of the two exceptions, one received $20,000 in cash, the limit of MSSIC's coverage; the second was unknown, since his deposit had never been entered in the association's books by the defaulting employee. This last depositor will also be paid in full upon receipt of appropriate instructions from the circuit court.

It thus appears that MSSIC's existence is not only theoretically an instrument for the public good and welfare but also practically justifiable. The citizens of Cumberland, Md., who were depositors in an insolvent savings and loan association will remember Christmas 1963 as demonstrative of this simple truth.

THE REPORT OF THE FEDERAL HOME LOAN BANK BOARD DATED JULY 16, 1963

A report filed with the Bureau of the Budget by the Federal Home Loan Bank Board (the Board) dated July 16, 1963, recommended against the enactment of H.R. 4297. The Board gave four principal reasons in support of its position. These reasons are listed below, together with the response of Maryland Savings-Share Insurance Corp. in connection with each point:

I. The Board contended failure of any State-authorized insurance fund may have adverse repercussions on the Federal Savings and Loan Insurance Corp. and institutions insured by it.

The corporation's response: This reason assumes that State-authorized insurance funds will fail in the future. There is no evidence to support this conclusion. To the contrary, all of the available facts support the position that the State-authorized insurance funds are more stable and conservative than the Federal Savings and Loan Insurance Corp.

The Ohio Deposit Guarantee Fund has operated at a profit since its inception; it now has a reserve fund in excess of $1,079,000 and total assets in excess of $10,000,000.

The Maryland Savings-Share Insurance Corp., in its first full calendar year of operation, had a profit of $17,543.66; total assets of $2,129,038.86; and a surplus of $18,577.76.

Both the Ohio Deposit Guarantee Fund and the Maryland Savings-Share Insurance Corp. are operated by experienced savings and loan people. Each corporation combines at least as much, and probably more, experience in the savings and loan field than the membership of the Federal Home Loan Bank Board.

The bylaws, rules, and regulations of the Maryland Savings-Share Insurance Corp., which are binding upon all associations insured by the corporation, require the maintenance of safe and sound management and fiscal policies by all members. To qualify as an insured member, each association must agree to maintain a liquidity fund of 6 percent and a reserve account of 6 percent; they must file complete fiscal information with the corporation at least annually. That membership in Maryland Savings-Share Insurance Corp. is limited to only the better operated associations is shown by the fact that of a total of 238 associations applying for membership, only 164 have been accepted.

A comparison of the Maryland Saving-Share Insurance Corp. and its insured members with the Federal Savings and Loan Insurance Corporation and its insured associations will demonstrate the fallacy of the Board's position. It is reliably reported that member associations in FSLIC have a ratio of reserves to invested capital of approximately 8 percent. The corresponding figure for mem-

ber associations of MSSIC is 12.85 percent. The ratio of FSLIC reserves to insured savings at June 30, 1964, is estimated to be 1.20 percent. The comparable figure for MSSIC is currently 1.808 percent, but this figure will increase to 2 percent and over when each member has contributed its full capital share. It thus appears that Maryland Savings-Share Insurance Corp. and its member associations are in a stronger current position than are Federal Savings and Loan Insurance Corporation and its insured associations, a fact totally ignored or overlooked by the Board's report.

II. The Board contended the risk upon State-authorized funds would be greater than on the Federal Savings and Loan Insurance Corporation because of the size and class of institutions insured by each.

The corporation's response: The factual basis for this point is disputed.

There have been many federally insured savings and loan associations that have been placed into either receivership or conservatorship by the courts. As a result, the Federal Savings and Loan Insurance Corporation has been required to spend large sums of money for the purpose of honoring its insurance commitments. For example, in the year 1963 the Federal Savings and Loan Insurance Corporation sustained a net insurance loss of $16,518,998. As of July 16, 1964, the Federal Savings and Loan Insurance Corporation had merged or taken under supervision eight associations in greater Chicago with total assets of $144,500,000, and, although the loss cannot be determined at this time, it is believed to be in excess of $50 million.

The Ohio Deposit Guarantee Fund, which has been in existence since January 1, 1957, has never been called upon to make advances or give financial assistance of any kind to its members.

In Maryland, insured members of Maryland Savings-Share Insurance Corp. restrict their mortgage lending to conventional home mortgages. They make no home improvement loans; their commercial lending is almost nonexistent. To the contrary, federally insured associations engage in home improvement lending; they may have as high as 18 percent of their assets in commercial loans. The facts make it clear that the associations insured by the existing State-authorized funds are as safe as, and probably safer than, those insured by Federal Savings and Loan Insurance Corporation.

III–A. The Board contended the Maryland Savings-Share Insurance Corp. is essentially a privately operated corporation without any real public control.

The corporation's response: The factual basis for this point is disputed.

The Maryland Savings-Share Insurance Corp. is a quasi-public corporation having a legislative charter. The corporation is not an ordinary business corporation (a private corporation) formed under the general provisions of article 23 of the Annotated Code of Maryland (the corporation article). By law, the corporation is required to file its bylaws, rules, and regulations with the Maryland Department of Assessments and Taxation. No amendment can be made in these bylaws, rules, and regulations unless approval thereof is first obtained from the director of the Maryland Department of Building, Savings, and Loan Associations.

The Governor of Maryland is required by law to appoint 3 of the 11 directors of MSSIC, and these individuals represent the State on the board.

No association may become a member of MSSIC until it has been certified for membership by the Maryland Department of Building, Savings, and Loan Associations. All examinations of such associations preliminary to membership in MSSIC are conducted by State examiners.

The director of the Maryland Department of Building, Savings, and Loan Associations attends all meetings of the board of directors of MSSIC as well as meetings of its membership committee. Copies of all determination or status letters sent by the Maryland department to any member of MSSIC are also sent to the corporation. The files of the Maryland department are made completely accessible to MSSIC, and duplicate files of member associations are given to MSSIC upon request.

The corporation has been permitted to use a seal which closely resembles in form and structure the great seal of Maryland, such permission being granted by an opinion of the attorney general of Maryland dated November 13, 1962.

Thus, Maryland Savings-Share Insurance Corp. is not "essentially privately operated without any real public control," as stated in the Board's report.

III–B. The Board contended: No provision is made for examination of or control over insured associations by Maryland Savings-Share Insurance Corp.; no provision is made in the Maryland statute for terminating insurance where an institution is pursuing an unsound course.

The corporation's response: Section 161–MM of article 23 of the Annotated Code of Maryland (1957 ed., and 1961 supp.) provides that the board of directors of Maryland Savings-Share Insurance Corp. may adopt and promulgate bylaws, rules, and regulations which conform to the intent and purpose of the act which established the corporation. The law further provides that the rules and regulations shall apply to members of the corporation and to associations applying for membership. The bylaws, rules, and regulations duly promulgated must be filed with the State department of assessments and taxation. From this, it follows that the bylaws, rules, and regulations of Maryland Savings-Share Insurance Corp. have legislative sanction and therefore have the force and effect of law.

The Maryland Savings-Share Insurance Corp. has adopted bylaws, rules, and regulations and has filed this material with the State department of assessments and taxation as required by law. These bylaws, rules, and regulations provide, among other things, the following:

(1) That the financial condition of all associations applying for membership in the corporation shall be examined by the department of building, savings, and loan association and, if necessary, by a representative of the Maryland Savings-Share Insurance Corp.

(2) That each member association shall file such fiscal reports and statistical information as the board of directors of Maryland Savings-Share Insurance Corp. shall require from time to time.

(3) That each association shall maintain safe and sound management and fiscal policies and shall comply with the laws of the State of Maryland and the orders and directives of the director of the Maryland Department of Building, Savings, and Loan Associations and the recommendations of the membership committee of the Maryland Savings-Share Insurance Corp.

(4) That the Maryland Savings-Share Insurance Corp. may expel any member from membership and terminate its insurance if the member is conducting an unsafe or unsound practice in the conduct of its business or if such member is violating any of the bylaws, rules, or regulations of the corporation.

It thus appears that, contrary to the assumption made by the Federal Home Loan Bank Board, validly adopted and legally binding legislative regulations of Maryland Savings-Share Insurance Corp. do make adequate provision for "termination of insurance where an institution is pursuing an unsound course."

IV. The Board contended: Because of disparities in face amount of insurance, State-authorized insurance programs for savings and loan associations might in the future be established and used as competitive devices inconsistent with the object of insuring accounts to promote stability.

The corporation's response: If this statement is taken at face value, it means, in essence, that the Federal Home Loan Bank Board opposes H.R. 3297 because Maryland Savings-Share Insurance Corp. imposes a threat of competition to the Federal agency.

The objectives of Maryland Savings-Share Insurance Corp. do not embrace any competitive purposes with either the Federal Savings and Loan Insurance Corporation or any other Federal or private entity. Maryland Savings-Share Insurance Corp. was formed as a quasi-State agency to fulfill a genuine need in the Maryland savings and loan industry. Its creation represents an effort on the part of a sovereign State to solve its internal affairs without recourse to governmental aid or subsidy.

It is regrettable that fear of competition should motivate the opposition to H.R. 3297 currently advocated by the Home Loan Bank Board. The purposes and objectives of MSSIC are the same as those of FSLIC. The board of directors of MSSIC wishes to cooperate with—not compete with—the appropriate Federal authorities to the end that stability and safety will be instilled in all savings and loan associations doing business in Maryland.

REASONS FOR PASSAGE OF H.R. 3297

No extended recitation is needed to demonstrate the benefits that will accrue to Maryland Savings-Share Insurance Corp. from the passage of H.R. 3297. The greater the surplus accumulated by MSSIC, the greater the protection it can afford to the people of Maryland who have entrusted their savings to its member associations. If MSSIC is required to pay Federal income taxes, however, its surplus will grow only half as fast. No useful purpose would be served

in this presentation to further elaborate this admitted and self-evident fact. For the following reasons, therefore, we urge the committee to give a favorable report to the subject bill:

1. *The public welfare.*—MSSIC performs a useful, public function without governmental subsidy or grants of any kind. It is a prime example of people helping each other through mutual effort. It is an integral part of the program of a sovereign State to correct a disastrous situation which befell its people. Its program is demonstrably workable. It adds another safeguard in an area which is of paramount concern to government everywhere—the protection of the savings, in some cases the life savings, of the people.

2. *Discrimination.*—All that Maryland asks from the Congress is to be afforded the same, identical treatment that the Federal Government now affords the people of Ohio. As stated previously, MSSIC was inspired by and patterned after the Ohio fund. An unconscionable discrimination would result if the Ohio fund were to remain tax free and its exact counterpart, Maryland Savings-Share Insurance Corp., were to be subject to tax.

3. *The Federal revenue.*—H.R. 3297 has, obviously, no impact on the Federal revenue. The bill—and a similar measure that was introduced into the 87th Congress—has twice been given careful and detailed study by the Treasury Department. A favorable report has been made in both cases. The report of the Treasury Department on a tax measure is entitled to paramount consideration. We ask that the report of the Department in this case be sustained by this committee.

The CHAIRMAN. Any questions?

Senator DOUGLAS. Sir, I regret that I was not able to hear the first part of your testimony. I was at a meeting of the Banking and Currency Committee of which I am also a member.

I notice in your statement you say that as of the 1st of May 1964, the Maryland Savings-Share Insurance Corp. had 164 members with total assets of $144.8 million. May I ask if these savings and loan associations had ever been insured under the Federal Savings and Loan Insurance Corporation?

Mr. CASE. No, sir, Senator Douglas, they had not been.

Senator DOUGLAS. Had they applied for membership for any insurance?

Mr. CASE. Whether they had applied or not is something that I really would not be able to say because I do not know the details of each of the associations. But I would be safe in saying to you, sir, that certainly 99 percent of them had not applied.

Senator DOUGLAS. Had not applied?

Mr. CASE. No, sir.

You see, Senator Douglas——

Senator DOUGLAS. Do you know why they had not applied?

Mr. CASE. Yes, sir. The reason why they had not applied, by and large, is because they are small, usually 1-day-a-week associations, which would not qualify under the limits that the Federal Savings and Loan Insurance imposes: these being, first, a total of $3 million in free share of capital; secondly, the ability to maintain an office 5 days a week; and, thirdly, to have this office on a ground floor location.

Now, many of these associations, Senator, are old-line regional associations located in Baltimore City which were really, many of them, ethnic in character. They were Polish, Jewish, and German, and so on, which meant 1 night a week or maybe 1 day a week, and were a relatively small size, maybe a quarter of a million to half a million dollars.

Senator DOUGLAS. Were any of these members in the so-called Mensik Tangiers Insurance Co.?

Mr. CASE. No, sir. I can say that without equivocation, absolutely not.

Senator DOUGLAS. We have our troubles with the savings and loan associations.

Mr. CASE. Yes, sir; I know you have.

Senator DOUGLAS. So I am not going to point the finger of scorn at Maryland except to say that the Federal Savings and Loan Insurance Corporation has, I think, exercised a healthy influence with respect to the boards of the savings and loan associations. It is not always as vigorous as it should be but, on the whole, it has been a healthy influence.

Are you at all fearful that a mutual directed by these local associations will be less stringent in its examinations than the FSLIC?

Mr. CASE. We have been told that our examination is more stringent and, I might say in that connection, it is my information that examinations are made by FSLIC on the average of about once every 18 months, whereas it is anticipated that the Maryland Savings-Share Insurance Corp. will examine its members on at least a yearly basis.

We have a program of continuing contact with 164 associations who are members of our corporation through our executive vice president, and since they are in a relatively constricted area it makes it possible for frequent contact not only in a personal but in a supervisory manner.

Senator DOUGLAS. Are these primarily Baltimore institutions?

Mr. CASE. Yes, sir; I would say 90 percent of them are located in Baltimore City.

Senator DOUGLAS. And ethnic and neighborhood institutions?

Mr. CASE. In many cases that is true, sir.

Senator DOUGLAS. Perhaps, if these general provisions, suggested by the Senator from Tennessee, are granted, you might have all kinds of private mutuals forming all over the country which would take in the weak savings and loan institutions, and with a less rigid inspection system might, therefore, lead to a breakdown? Are you at all fearful of that possibility?

Mr. CASE. Senator Douglas, I am not sufficiently knowledgeable about the situation that exists throughout the United States to give you anything other than my opinion on that point, which would be only my opinion. I seems to me, first—if you care to have my opinion——

Senator DOUGLAS. Yes; of course.

Mr. CASE (continuing). That this danger is more imaginary than real for a number of reasons.

First, in most of the other States of the Union you have, of course, you had regulation, and in many States this regulation has been very good. Therefore, the smaller State-chartered associations have, by and large, been under a fairly strict type of surveillance as distinguished from——

Senator DOUGLAS. Do you think that is really true?

Mr. CASE (continuing). Well, we found—I was also chairman of the commission which examined into and recommended the regulatory act; and we, of course, looked at all of the regulatory acts throughout the country.

Now, whether in practice these acts are carried out or not I do not know. But as a matter of substance on the lawbooks, many of them are very, very good.

Senator DOUGLAS. If I may speak from experience about my own State, we had a gentleman as State auditor by the name of Orville Hodge, of whom some of you may have heard, who succeeded in getting through the legislature a bill permitting State mutuals to convert themselves into State stock associations. The trouble which we have had and are continuing to have, with many savings and loan institutions, has been almost uniformly—I think there are one or two exceptions to this—confined to State savings and loan banks rather than to federally chartered ones. Also, there has been a high degree of deterioration on the mutuals converted into stock associations.

Mr. CASE. There you have a very good point.

Senator DOUGLAS. What is that?

Mr. CASE. There you have a very good point.

Senator DOUGLAS. Yes.

Mr. CASE. This cannot be done in Maryland. Our law prohibits it. There can be no stock associations.

But may I say, Senator Douglas, in connection with your other statement, and not seeming to contradict you——

Senator DOUGLAS. I am not speaking about Maryland. I am only speaking about my own State.

Mr. CASE. No; and I should like to say something about Illinois, too, if I may.

It is my understanding that three of the largest associations which have had financial difficulties in your State are federally insured, they being Hillside Savings & Loan Association——

Senator DOUGLAS. Which?

Mr. CASE (continuing). Which had assets of about $17——

Senator DOUGLAS. Hillside?

Mr. CASE (continuing). $17¾ million.

Senator DOUGLAS. Yes, Hillside, I grant you that.

Mr. CASE. Property Federal Savings & Loan.

Senator DOUGLAS. What was the other one?

Mr. CASE. Property Federal Savings & Loan Association which had assets of $5 million.

Senator DOUGLAS. Are they suspended?

Mr. CASE. Well, they have been—they are ones that have been—reported difficulties, as I understand it.

First Federal Savings & Loan Association.

Senator DOUGLAS. That is a huge one.

Mr. CASE. Which was merged into the Second Federal Savings & Loan Association having assets of——

Senator DOUGLAS. Yes.

Mr. CASE (continuing). Which had assets of $6 million.

Senator DOUGLAS. Are you speaking of the famous First Federal, which has deposits of well over $300 million?

Mr. CASE. My information is that the First Federal Savings & Loan Association of Morton Grove had assets of $6 million and was merged by FSLIC into another one so these three are very large Illinois firms.

Senator DOUGLAS. Have the last two gone into liquidation?

Mr. CASE. No, sir. I understand that they have been merged by FSLIC to prevent liquidation.

Then, of course, there are a number of others.

Senator DOUGLAS. Well, I think the general statement is true; the incidence of loss has been greater in the case of the State savings and loan institutions than in the case of the Federal institutions. But the conversion of mutuals into stock companies has lessened the care with which they have been managed, and even though I congratulate you on having such a prohibitory law in Maryland, the law can always be changed.

Mr. CASE. Well, that certainly is true, sir. It is rather difficult to get it through, and we fight like tigers before we would permit a change.

Senator DOUGLAS. That is all, Mr. Chairman.

The CHAIRMAN. Senator Carlson?

Senator CARLSON. Mr. Case, you are chairman, I believe of the board of the Maryland Savings-Share Insurance Corp.?

Mr. CASE. Yes, sir; that is correct.

Senator CARLSON. Who composes it, the directorship, of this organization?

Mr. CASE. The directorship of the corporation, Senator, is composed of eight men who are representatives of member associations.

Now, both of those words are, in effect, words of art and, therefore, let me define them. A member association we have already talked about is one who has been examined, and so on, and is part of the organization.

Senator CARLSON. And a part of this corporation.

Mr. CASE. Yes, sir.

A representative of that member is an officer or director or attorney of the member who has been designated as representative by the member association.

The bylaws provide that there shall be eight of these people selected as members of the board.

Senator CARLSON. By whom?

Mr. CASE. By the membership voting at its annual meeting.

The law also says that the Governor of Maryland shall appoint three public members to the board for 4-year terms and they, of course, can be reappointed.

If you wish me to follow the directorship a little further, the bylaws provide further that the member associations' representatives can serve two terms and then they must give way to others.

The corporation's bylaws also provide for a membership committee of the board which, in addition to directors, has two other persons who are representatives of member associations, and they sit with the membership committee and attend board meetings but cannot vote.

Senator CARLSON. Then if I understand correctly, out of this group of the board of directors, the really truly public representatives would be limited to three people?

Mr. CASE. Well, in the sense that they do not have to be representatives of member associations that is correct, sir.

Senator CARLSON. So the public representation of those people who invest their money in the associations is limited to these three people largely?

Mr. CASE. Well, the safety of the people's money is very much the concern of every man on that board, sir.

Senator CARLSON. I appreciate that very much. But the point is that I—and, of course, I am not familiar with this, but I think it is only natural that you would get back to your own State in——

Mr. CASE. Yes, sir.

Senator CARLSON (continuing). In dealing with these problems, and I have had the honor of serving as the Governor of a State myself. But this happened before I became Governor some years back. We established a State bank guarantee law, one of the first in this Nation, pretty much along the lines that you have established the guarantee of the savings and loan associations. When the difficulties arrived, the thing, of course, went into bankruptcy. It was not based on the faith and credit of the State. Many people had placed their money in these banks on the theory that they were protected, and they found out they were not, to their dismay and to the regret of many of us and, therefore, I am greatly concerned about the creation of agencies of this type without more back of it than the institutions themselves, because in our own State we had a number of bankers who would not enter into this guarantee program. They contended that they were prudent bankers, and they intended to conduct their banking facilities, and this operation of the guarantee let some people be a little loose in handling some of their operations and they got into difficulty.

There is one problem that comes into my thinking when I think about your problems today, and I appreciate your problems in Maryland. I shall, at least, keep an open judgment on this.

The CHAIRMAN. Senator Gore?

Senator GORE. Do you hold in any way a position with the government of the State of Maryland?

Mr. CASE. No, sir. I am sorry, I do. I am a member of the board of regents of the University of Maryland.

Senator GORE. Is the institution for which you now speak in any sense an institution of the government of Maryland?

Mr. CASE. We think it is a quasi-governmental agency, Senator. It is not an instrumentality of the State of Maryland.

Senator GORE. If it is not an instrumentality of the State of Maryland, then it is private.

Mr. CASE. Well, there is a shade of difference between what you are saying, I think, and what the true fact is. I would say it is a quasi-public corporation. This is the way the Treasury Department has defined it, if not in writing at least to me in person, and this is the way the Ohio, Massachusetts, and New York funds are grouped.

Senator GORE. Does the government of Maryland have any stock in it?

Mr. CASE. No, sir.

Senator GORE. Does the government of Maryland have any control over it?

Mr. CASE. Yes, sir; very considerable control.

Senator GORE. Does the government of Maryland share in any of the profits or benefits from it?

Mr. CASE. On the benefit that the people of Maryland's savings are protected to a higher degree.

Senator GORE. Well, there might be some results not beneficial. Would the State of Maryland be liable in any respect for the losses of this corporation?

Mr. CASE. The law says, as now written, that the faith and credit of the State is not pledged to the obligations.

Senator GORE. Then it does not perform a public function for the government of Maryland. Since the faith and credit of the State of Maryland are not pledged, it must be private unless you could say that its mutuality in some way alters its private character or so it would seem to me.

Mr. CASE. Well, it would equally seem to me that as the Treasury Department and others who have dealt with this subject through the years have said, it is a quasi-public corporation.

Senator GORE. You are aware, are you not, that after many false starts, with much trouble and controversy, the Congress has finally made a start in taxing the profits of cooperatives and mutual concerns, including savings and loan associations and mutual insurance companies?

Mr. CASE. Senator Gore, I am very familiar with that, sir.

Senator GORE. But now you ask us to reverse the trend and provide complete tax exemption for this corporation.

Mr. CASE. No, sir. I ask you only to afford Maryland the same exemption you have heretofore afforded the State of Ohio.

Senator GORE. Then, because the Congress erred in providing such tax exemption to corporations in the State of Ohio, you would urge us to repeat the mistake with respect to Maryland. Would you then be prepared to support the same thing with respect to Tennessee, New York, and other States?

Mr. CASE. Senator Gore, I would say, first, in answer to your question, that I do not believe it was an error. I think the public good is well served by this type of non-Federal situation where the public's money is not involved, and I think it is a good thing not only for our State but for our country as well to have associations of this kind where people can get together and, in a sense, do as they used to in the olden days in the matter of self-self. I think that this is good.

But with reference to your specific question——

Senator GORE. Self-help without taxation.

Mr. CASE. That is right. This is a situation which——

Senator GORE. Suppose that you and I organized one in the District of Columbia.

Mr. CASE. Well, we could not for several reasons, but I am coming to the burden of your question, sir.

Senator GORE. Let us go down to Tennessee, and suppose we organized one there.

Mr. CASE. I have spent many pleasant days in your State, sir.

Senator GORE. Self-help can be rather profitable sometimes. I have a feeling that we have a basic policy in this country for persons and corporations to pay taxes on income earned, realized.

Mr. CASE. Unless those corporations are serving such a public purpose which overrides the general tax philosophy of the United States.

Senator GORE. Well, now, that same argument was given here for years to exempt the cooperatives and the savings and loan associations from Federal taxation. We finally have moved in the direction of

some tax equity—not very far, it is true, but we have made a start in taxing cooperatives and mutuals on income realized.

Whether the Congress has gone far enough is beside the point here, but at least we made a start in that direction, and many people applauded the Congress for doing that. But you now seek to reverse that trend.

Mr. CASE. No, Senator, I do not seek to reverse it for this simple reason: cooperatives, mutual savings and loan associations, or stock associations, as Senator Douglas was talking about, all wind up sooner or later with somebody profiting, that is to say, the depositors, the officers, or somebody gets the benefit of this yield which we should call in, between us.

In this corporation nobody gets it because the law expressly states that it cannot be divided up and given back to anybody, so the difference, it seems to me, is abundantly clear.

What you have done, and what the Congress has done, in these other acts it has said, in effect, "Here is a type of situation which is, in effect, distributing gains and profits of some kind, and we think even though it is mutual, a tax should be applied because this is a distribution coming back to the people."

But in this corporation nothing comes back. It is completely—it is isolated by law and, therefore, I think there is a very great distinction between the cases you suggest and the one we have before the committee.

Senator GORE. Well now, you said no one benefits. Let us examine that just a little. As the profits of the corporation accumulate, what effect will the accumulation of profits, the assets of the corporation, have upon the insurance provided for its members by the corporation?

Mr. CASE. In amount it will have no effect, it will create a larger reserve fund, therefore, provide a safer vehicle, a larger vehicle, but the acount of insurance remains exactly the same.

Senator GORE. The cost of insurance is what I am referring to.

Mr. CASE. The cost, Senator Gore, is made up by the 2-percent deposit which is paid within a relatively short time after an association has become a member and, therefore, there is no continuing cost except as free share accounts are increased or decreased by the member association, in which event there is an adjustment of the capital deposit on a semiannual basis.

Senator GORE. Then, as the profits accumulate and assets grow there will be more insurance and better insurance provided at no extra cost.

Mr. CASE. I do not know what you mean by more and better. The amount will be precisely the same, $20,000, and if, as has happened in Cumberland last year, the free shareholder gets paid in cash, it is hard for me to see how it can be any better.

Senator GORE. If the reserves of the corporation are larger, the insurance is certainly more reliable, it it not?

Mr. CASE. It is only more reliable to the extent that additional calls on members would not, perhaps, have to be made in the case of the situation that Senator Williams discussed earlier in our meeting, but it would not be better, as I understand the use of that word.

Senator GORE. But it would be more beneficial to the members.

Mr. CASE. It would be more beneficial——

Senator GORE. Less liability, as you just said, on the part of the members.

Mr. CASE. In the sense they would not be called upon, perhaps, to pay additional capital contributions.

Senator GORE. And you said earlier that the faith and credit of the State of Maryland is in no way pledged to support this, so as the assests accumulate from the earned profits of the corporation, there would be ready reserves to provide the insurance, and less liability for a call upon the member associations. Would you say that was correct?

Mr. CASE. I would say that is correct; yes, sir.

Senator GORE. Now suppose that a member association wishes to enlarge and increase its operations. Does your law provide that they shall pay an additional premium?

Mr. CASE. Yes, sir; equal to—when you say enlarge, of course, I assume you mean that they get more free share accounts, because this is the only way a mutual savings and loan association can enlarge.

Senator GORE. Yes.

Mr. CASE. And the law does provide on a semiannual basis an adjustment of the capital deposit, either up or down, depending upon the amount of free share accounts outstanding.

Senator GORE. Are you aware of the history of the provision in the Federal income tax law which was written into the law for the benefit of a Catholic nun who wished to contribute practically all, if not all, of her income to charity? This provision, which was motivated by such a worthy cause, has become one of the largest loopholes of tax avoidance in our tax structure.

Mr. CASE. You are suggesting the annual 90-percent contribution act; yes, but I didn't know that was the genesis of it.

Senator GORE. Yes.

Mr. CASE. I am completely familiar with the act.

Senator GORE. That was the genesis of it.

Now, you have come in with a cause which, on the surface, seems worthy. But you propose that the Congress enact a general law. I am impressed with the suggestion Senator Doublas made as to the vast potentialities which we may not now be able to foresee, but of which I believe we should be forewarned, for the use of this provision, if written into law, by many corporations other than the one for which you speak and for purposes perhaps less commendable.

Mr. CASE. Senator Gore, my only answer is that is, of course, we all must be vigilant in the guarding of the revenue and also to insure that the social justice be done. But when a corporation receiving a State charter, as this one has, and doing what it has done is emulated in any other State under the exact same situations, it seems to me only fairness and justice would say that that other association should be afforded the same tax benefit.

Senator GORE. But it may not be the exact same situation.

Mr. CASE. The law as it is drawn today would certainly—you have, as a matter of fact, before you an amendment which is proposed to liberalize this act to permit other things which mutual banks might do—I am not here, of course, to speak to that, because I am having enough trouble with my own situation—but this is a very tight law, Senator Gore. It is pinned down to a point where I do not believe

you could find great abuse of it, as you suggest you might find in the future.

Senator GORE. Well, in response to a question by Senator Douglas, you acknowledged, of course, that the State of Maryland had changed the provisions of the existing law——

Mr. CASE. Well now——

Senator GORE (continuing). To comply with the bill now here proposed. I do not criticize that at all. But I just point out you did acknowledge that. Maybe I should not say acknowledge—you stated it. But other States which do not have the same State law which Maryland has could qualify, or organizations within other States not having the same law as Maryland, could qualify.

Mr. CASE. They could qualify, Senator.

My point is that they could qualify only under the strict Federal law. I was speaking of the Federal law which is strictly written, and which has been very strictly interpreted by the Internal Revenue Service. I am not talking about the ability of the Maryland Legislature or anybody else to change the law. This Congress can change within limits any law it cares to.

Senator GORE. Is there any reason why these member associations in Maryland could not obtain such insurance from the FSLIC?

Mr. CASE. Yes, sir. I might say at the outset it has nothing to do with their liquidity or soundness. What it has to do with is the size of the association, the frequency of the times when they meet, and usually the places at which they meet. In each of these areas, FSLIC has rather strict requirements or requirements that are not, cannot be, met by these associations.

For example, the $3 million requirement which I understand is the present requirement on free share accounts could be met by only a handful of the associations insured by Maryland Savings-Share Insurance Corp. because they are much smaller. They do not solicit deposits as such and, therefore, they have remained in the neighborhood in Baltimore. They are small neighborhood organizations is what they really are, many of them.

Senator CARLSON. Will the Senator from Tennessee yield at that point?

Senator GORE. Yes.

Senator CARLSON. I believe I have your report here, and I was interested in this, in view of what you are discussing. This sentence reads:

> Your corporation now has 162 members with total assets of $138,407,504.92.

Do I understand this would mean an average of less than $1 million each?

Mr. CASE. You mean a simple average?

Senator CARLSON. Yes; a simple average is what I mean.

Mr. CASE. Yes; they are very small.

Senator CARLSON. That gets into the size of it.

Senator GORE. Well, perhaps instead of giving tax exemptions Congress should consider lowering the requirements set by FSLIC.

Mr. CASE. Well, Senator, as Governor Tawes said, we in Maryland do not think that every association is a good association that is governed by Federal Home Loan Bank Board rules or insured by FSLIC.

Here is the situation where a State, a sovereign State, is seeking to work out its own problems and not come to Washington and ask for help.

Senator GORE. I am sorry to disagree with you there. If this were a corporation owned by the State of Maryland that would provide this public service it would be a different thing. But this is a corporation which will have investment income, and for which you are asking tax exemption. It is just that simple. True, it is organized under the laws of the State of Maryland, but so is every other corporation in Maryland.

Mr. CASE. You misunderstood me, Senator. What I meant was if you lowered the requirements or required the Home Loan Bank Board to lower the requirements for Federal insurance, then you might as much as double your budgetary requirements for examiners, for additional help of all kinds to make reports, and so on. And now, this would be a bigger Federal agency. All I am saying is, of course, we are here asking for tax relief, but all I am stating is that the situation we now present to you is one where we are not asking the Federal Government to get bigger in the sense of its agencies expanding. What we are saying is we think that this situation can be controlled at home. We are controlling it at home, and we would like to continue to control it at home.

Senator GORE. I have no objection to the State of Maryland exercising its regulatory power. To the contrary, I applaud it. I do not know why it was so late in starting. But asking for tax exemption is another thing.

Are you acquainted with the practice in the House Ways and Means Committee of annual members' bills?

Mr. CASE. No, Senator. You have gone past my amount of knowledge now.

Senator GORE. You do not know about this little club, this practice of members' bills?

Mr. CASE. No, sir; I do not.

Senator GORE. You do not know whether this was a members' bill or not?

Mr. CASE. This particular bill here?

Senator GORE. Yes.

Mr. CASE. Well, I can tell you what the bill was. I do not know what it was not. What it was was a bill that I personally asked Representative Fallon to introduce, and it was passed——

Senator GORE. I will ask no further questions.

Senator DOUGLAS. For the sake of the record, the comment of the Senator from Tennessee opens up great possibilities. I understand there is a principle in common law—the lawyers will correct me if I am wrong—that every dog is entitled to one bite.

Is the Senator from Tennessee implying that every member of the inner club of the Ways and Means Committee is entitled to one bill a year? [Laughter.]

Senator MCCARTHY. As a former member of that club I might say that sometimes we got two. We go around the committee twice. [Laughter.]

Senator GORE. Mr. Chairman, I do not know why there should be discrimination as between the two Houses of Congress. Have you

considered the possibility of permitting each member of the Senate Finance Committee to have a pet bill passed per year? [Laughter.]

Senator DOUGLAS. I am very glad to say that the chairman has not permitted this.

Senator GORE. I asked him if he had considered it.

The CHAIRMAN. We do not have any pet bills in this committee that I know of.

Senator MCCARTHY. I think I can make a defense of the House Ways and Means Committee. It has stood up on general measures very well.

Senator GORE. I am not talking about how they stood up on general measures, but talking about the members' bills.

Mr. CASE. Representative Fallon is not a member of the House Ways and Means Committee, if that adds to this discussion in any way.

Senator GORE. I was not making any reference to Congressman Fallon.

The CHAIRMAN. Senator McCarthy.

Senator MCCARTHY. How much money would be involved in this insurance fund if all the eligible savings and loan associations in Maryland would contribute 2 percent?

Mr. CASE. Yes, sir. I think it has about reached the optimum. I would think it might go maybe another $10 million, $15 million. But I believe that all of the associations that qualify for membership have come in, or practically all of them.

Senator MCCARTHY. How many of them are there?

Mr. CASE. 164 now, sir; and they have total assets, they are with total assets of $144 million.

Senator MCCARTHY. $144 million?

Mr. CASE. $144.8 million and we have got all of the good ones.

Senator MCCARTHY. This would be the equivalent of increasing their reserves by about 2 percent.

Mr. CASE. This would be a 2-percent contribution in cash to the insurance company is what it amounts to.

Senator MCCARTHY. It would be on top of the reserves which they are now allowed.

Mr. CASE. Yes.

Senator MCCARTHY. What are those reserves, 6 percent?

Mr. CASE. In Maryland they are required to be 6 percent.

Senator MCCARTHY. That is a tax-exempt reserve, is it not?

Mr. CASE. That is correct, sir.

Senator MCCARTHY. So this, in effect, would mean that you would have 8 percent total reserves, which would not be subject to tax.

Mr. CASE. Except that the 2-percent contribution, Senator, was not tax deductible.

Senator MCCARTHY. Yes, I understand.

Mr. CASE. This capital contribution is not tax deductible.

Senator MCCARTHY. What percentage of your savings and loans would be covered by this $144 million in assets?

Mr. CASE. I am informed by Mr. Wolf, who is a former director of the Department of Maryland's Building, Savings, and Loan Associations that he thinks it is about 70 percent.

Senator MCCARTHY. Seventy percent. Why would the others not be covered?

Mr. CASE. Some of those associations, Senator, are not in the business of taking money from the public as such. They are family corporations which have a very restricted free share list. This is one group that does not come in.

Senator MCCARTHY. Does the public know which of the savings and loans——

Mr. CASE. Sir?

Senator MCCARTHY. Does the public know which of the savings and loan associations in Maryland are this kind of tightly held family-type savings and loan associations or are all savings and loan associations under the same law?

Mr. CASE. If I understand your question correctly, it is do they know, does the public know, whether the associations insured by this——

Senator MCCARTHY. No, I assume they would know that. You probably would put up a plaque or something.

Mr. CASE. That is right, a symbol.

Senator MCCARTHY. But some of these companies would not come in. Could they not come in or would they not come in?

Mr. CASE. Anybody can come in who is a State-chartered savings and loan association.

Senator MCCARTHY. Why would the type of company to which you have just referred not come in, assuming that its financial condition was such that it would be eligible?

Mr. CASE. I have asked that question many times myself, and the answer seems to be that they are not interested in the public reaction. In other words, they are not soliciting or do not want free share accounts from the public and, therefore, the insurance—they know they are sound, they are conducting their own business in their own way. They may not want a second regulatory agency looking over their shoulders. These are several of the reasons suggested to me.

Senator MCCARTHY. Your more reputable savings and loan associations in Maryland would not come in?

Mr. CASE. Would not come in?

Senator MCCARTHY. Yes.

Mr. CASE. They are in.

Senator MCCARTHY. I thought you said these would not come in, and you said they had a good reputation and did not feel they needed the plaque.

Mr. CASE. No, because they are not searching for free share accounts, Senator.

I would say all of the well-known, reputable public savings and loan associations in Maryland are members of our corporation. I should certainly like to correct the record if I misstated that one.

Senator MCCARTHY. Yes. The point is they are not seeking free share accounts.

Mr. CASE. Yes, sir.

Senator MCCARTHY. That is the point. Reading your report of the Old Line Savings & Loan Association in Cumberland, in which was discovered that an employee had appropriated $50,000 of the funds and that this threw the association into insolvency, they must operate on a very thin margin.

Mr. CASE. It was a small association with $250,000.

Senator McCarthy. How could she get away with $50,000 in an operation of that kind?

Mr. Case. That is a very good question. The lady, who has since been convicted by the circuit court for Allegany County, and is now awaiting sentence, was a pretty clever operator. She, the accountants explained it to me in what I would call kiting, but she would take your deposit and enter it under Senator Byrd's name and so on down the line until all accounts would seem to balance, but at one time the house of cards fell in, and that was the end of that.

Senator McCarthy. $250,000, she must have really run kind of a whirling account.

Mr. Case. Well, she would take just in small amounts—in other words, you would come in and make a deposit. She would put the deposit in her pocket, enter it into somebody else's account. Somebody else would come in and she would make a deposit in your account and put it in her pocket or when mortgages were paid off, and this was one of her real ways of handling it, she would take that money and instead of entering it correctly into the passbook she would take the mortgage runoff and put it in her pocket. So the true unpaid principal balance of the mortgage and the books of the corporation revealed different figures.

Senator McCarthy. How many savings and loan associations do they have of that size, $250,000, or under $1 million?

Mr. Case. Mr. Wolf informs me, who, incidentally, is the executive vice president of Maryland Savings-Share Insurance Corp., that there are between 50 and 75.

Senator McCarthy. How many?

Mr. Case. Between 50 and 75.

Senator McCarthy. Out of what total?

Mr. Case. About 50, Senator, of the 164.

Senator McCarthy. About a third of them.

Mr. Case. Yes, sir.

Senator McCarthy. Are there any other States in which that situation exists or is Maryland somewhat unique in the number of very small associations?

Mr. Case. Well, as I mentioned earlier in response to some questions Senator Douglas asked me, because of the way these associations grew in the neighborhoods in Baltimore City, it would be surprising for me to find that you would have in many States, certainly, where this situation exists.

Senator McCarthy. I have no further questions, Mr. Chairman.

Senator Gore. One other question. Is this 2-percent capital contribution a requirement of State law or of the corporation?

Mr. Case. The corporation, sir.

Senator Gore. Then if the assets of the corporation, with tax exemption, accumulated, the corporation could lower that to 1 percent.

Mr. Case. No, Senator Gore, it could not for this reason. The 2 percent has already been paid, you see.

Senator Gore. I mean for new associations or future expansions of existing associations.

Mr. Case. No, sir; that to me would be discrimination which we could be enjoined from doing. I do not think we could give——

Senator GORE. Certainly the Federal Government, the U.S. Government, would have no control over that. Whether it was 2 percent or two-tenths of 1 percent; you could still qualify.

Mr. CASE. The United States does not have any control over the amount of the capital deposit, this is perfectly true.

Senator GORE. So taking it to admittedly an absurd extension, you would ask to be provided under this bill tax exemption although your assets might accumulate to such an extent that any new association or expansion of the existing member association could have insurance for the ridiculously low rate of two-tenths of 1 percent capital contribution.

Mr. CASE. This, I think, would be something that could not be provided by the corporation.

Senator GORE. Well, so far as the Federal law is concerned.

Mr. CASE. So far as the Federal law is concerned; yes, sir. Because the Federal law——

Senator GORE. Don't you see, then, what a trap you are asking us to enact?

Mr. CASE. Well, Senator, I must say that I do not see the trap. I think it is, this law has been, operating since 1951. It has been applied in the State of Ohio where the exact same thing we are asking is going on every day. I do not think anyone has ever suggested that the Ohio situation is a trap in any way. Therefore, I fail to see, with all due respect to you, sir, a trap here.

Senator GORE. Thank you, Mr. Chairman.

Senator CARLSON. I have no further questions.

The CHAIRMAN. All right.

Senator DOUGLAS. One of the practices of Mr. Mensik, who has not been a credit to the State of Illinois, and whose influence in the State of Maryland was not very good either——

Mr. CASE. A feeling we share with you.

Senator DOUGLAS (continuing). Was to put signs in the window which were not precisely untruthful, but which did not convey the full truth. As I remember it, he would say the accounts were insured, and this gave the impression that they were insured in the Federal Savings & Loan Insurance Corporation.

My memory goes back also to 1929. I visited New York City a number of times that summer, and I would go by the branches of the Bank of the United States. It did its business with immigrant groups largely, and I do not know whether people thought they were depositing their money in the Third Bank of the United States or not, but there were very large accounts. While I think the later opprobrium which was cast upon the bank, and upon Mr. Isidore J. Kresel, its attorney, was in many respects highly exaggerated, nevertheless, I think this was the first bank which failed in New York in the depression which followed.

Now, I notice in your prepared statement that you state that the law has some restrictions about the advertising symbol which is to be used.

Mr. CASE. Correct, sir.

Senator DOUGLAS. I am not clear what it is, and I am not quite clear whether it is adequate. I wondered if you would explain that?

Mr. CASE. Yes, sir; I would be very happy to. We also were quite conscious of Mr. Mensik and the Securty Financial Insurance Co., I think is what he called it, organization; and therefore, when the Maryland Savings-Share Insurance Corp. got underway it was the consensus of the board, later made into a rule, that no statements concerning the insurance coverage of the Maryland Savings-Share Insurance Corp. could be made without the prior written approval of the board of directors, either by a special or by a general resolution.

Senator DOUGLAS. The board of directors of the mutual——

Mr. CASE. Of the insurance company.

Senator DOUGLAS. Of the mutual insurance company.

Mr. CASE. Yes, sir; of the insurance company.

Senator DOUGLAS. In other words, they are self-regulated.

Mr. CASE. Perhaps I did not make myself abundantly clear, Senator. No savings and loan association can make any representation about this insurance unless it gets permission from the board of directors of the insurance company. It cannot say anything about it at all.

Senator DOUGLAS. And what do the present provisions say?

Mr. CASE. The present provisions are that it may display the seal and say——

Senator DOUGLAS. The seal?

Mr. CASE. The symbol.

Senator DOUGLAS. The symbol.

Mr. CASE. Which is on the copy of the rules and regulations, if you have a copy before you, Senator. They may display that symbol, and it may say, in effect, "This corporation is insured by the Maryland Savings-Share Insurance Corp. created under the laws of the State of Maryland." And that is all. This problem was one which we were completely conscious of, Senator Douglas.

Senator DOUGLAS. That is better than the previous absence of provisions which permitted Mensik to disguise the insurance of the Tangiers Co. as protective.

But I wonder if it is adequate, particularly since this serves, as you say, foreign language groups? Now, granted that they have had time to become assimilated in the population, but does not that look quite formidable?

Mr. CASE. The seal, sir?

Senator Douglas. Yes.

Mr. CASE. Well, I hope it is considered to be a symbol of safety and trust in our State.

Senator DOUGLAS. But this could be changed by the decision of the board of directors of the MSSIC?

Mr. CASE. It could be changed by the board, but only with the approval of the State regulatory authorities.

Senator DOUGLAS. I see. Thank you.

The CHAIRMAN. Thank you very much, Mr. Case.

Mr. CASE. Thank you, Senator.

Senator GORE. Mr. Chairman, I must depart. I would like to request that the Chairman of the Federal Home Loan Bank Board be asked to testify with respect to this bill.

The CHAIRMAN. The Chair has already placed in the record the formal report of the Federal Home Loan Bank Board, which was submitted in lieu of appearing.

The next witness is Mr. Rabstejnek of the Savings & Loan Bank of the State of New York.

Senator Javits hoped to be here to present you, but was detained. His statement will be put in the record.

(The prepared statement of Senator Javits follows:)

STATEMENT OF SENATOR JACOB K. JAVITS IN SUPPORT OF AMENDMENT TO H.R. 3297

The amendment which I have submitted to H.R. 3297, with the cosponsorship of my colleague Senator Keating, and of Senator Beall, relates only to the taxable status of the Savings & Loan Bank of the State of New York.

The Savings & Loan Bank of the State of New York is a quasi-governmental institution created by the New York Legislature for the purpose of providing reserve funds for domestic building and loan associations. It is believed that the Savings & Loan Bank of the State of New York is the oldest organization of its kind, having been in continuous operation for almost 50 years. During this period, it has performed the vital function of insuring stability for an important aspect of our State banking system.

From its inception, the bank has been exempt from New York income tax. And until very recently when the Revenue Service revoked an administrative ruling of long standing, the bank has also been exempt from Federal income tax.

The bank performs substantially the same functions for its member associations in the State of New York as the Federal home loan banks perform on a Federal level. The Federal home loan banks are exempt from all State and Federal tax. H.R. 3297, with this amendment, will extend the same tax treatment to the Savings & Loan Bank of the State of New York as the Federal home loan banks presently enjoy, and will correct an apparent legislative oversight at the time the Congress enacted legislation exempting from income tax, organizations similar to the Savings & Loan Bank of the State of New York.

I would like at this time to introduce to the committee the distinguished president of the bank, Mr. Otto J. Rabstejnek, who will testify in detail on the amendment which I very much urge the committee to adopt.

The CHAIRMAN. Also Congressman Keogh has indicated his interest in the legislation.

Will you proceed, sir?

STATEMENT OF OTTO J. RABSTEJNEK, PRESIDENT, SAVINGS & LOAN BANK OF THE STATE OF NEW YORK; ACCOMPANIED BY JOHN T. SAPIENZA, ATTORNEY

Mr. RABSTEJNEK. Mr. Chairman and members of the committee, my name is Otto J. Rabstejnek. I am president of the Savings & Loan Bank of the State of New York and I am speaking today on behalf of the amendment to H.R. 3297 cosponsored by the distinguished Senators from New York, Mr. Javits and Mr. Keating, and the distin-

guished Senator from Maryland, Mr. Beall. My oral statement will be as brief as possible.

I am accompanied by our Washington counsel, Mr. John T. Sapienza. I am speaking as briefly as possible, but I ask that my appendixes be made a part of the record.

The Savings & Loan Bank of the State of New York was created by an act of the Legislature of the State of New York in 1914 and commenced operating in 1915 as the Land Bank of the State of New York. The present name was acquired as a result of an act of the New York State Legislature in 1932.

From the date of its inception, the Savings & Loan Bank has been a creature of the New York State Legislature. Proposed bylaws for the bank the general powers of the bank and the restrictions on such powers as well as the composition of the bank's membership and the number and election of the bank's directors are all specifically regulated by statute. The Savings & Loan Bank, together with its capital, accumulations, and other funds, is exempt from State taxation under section 446, article 10-B of the New York State banking law.

The Savings & Loan Bank is organized without capital stock and membership is limited to savings and loan associations in New York. It is authorized to extend credit to, and act as a service bank for, its member savings and loan associations operating within the State of New York.

In the creation of the Federal home loan bank system, the creators of the Federal system called upon the nearly 20 years of experience of the Savings & Loan Bank in this field, the only State institution of its type, then as now, in existence. The Savings & Loan Bank of the State of New York was the prototype of the Federal system.

The tax-exempt status of the Federal home loan banks was established by Federal statute when the system was created. The Savings & Loan Bank was officially recognized as a tax-exempt organization by a ruling of the Internal Revenue Service in 1935. Congress, in 1951, eliminated the tax-exempt provisions for domestic building and loan associations but expressly provided for a tax-exempt status for State-chartered insurance and liquidity funds in what is now section 501(c)(14).

The language of this provision was made to order for situations then existing in the States of Massachusetts and Connecticut. Through inadvertence, no consideration was given to the Savings & Loan Bank of the State of New York. Nevertheless, we believed that we were tax exempt and the Internal Revenue Service, by letter dated December 1, 1962, reaffirmed our tax-exempt status.

In December 1961, the Internal Revenue Service notified the Savings & Loan Bank of its intention to revoke the banks tax-exempt status on the grounds that the Service had erred in reaffirming the bank's tax-exempt status in 1952. It considered it had erred because the Savings & Loan Bank did not insure accounts in savings and loan associations but only provided reserve funds.

It is apparent that the Savings & Loan Bank of the State of New York has been the victim of an unintentional legislative oversight. The language of section 501(c)(14) was added at the behest of the mutual deposit guarantee funds in Massachusetts and Connecticut

with no thought being given to New York. The Ohio Deposit Guarantee Fund which did not qualify under the 1951 provision was granted tax exemption in 1960. No relief was considered for New York because our bank had been granted tax-exempt status under this section by a special ruling of the Internal Revenue Service.

The organizations which are tax exempt under section 501(c)(14) provide two services for their member banks. First, they provide a deposit insurance fund to aid their members in financial difficulties. Second, they maintain a liquidity fund to make loans to members which are basically sound but short of liquid assets. The deposit insurance function is performed under Federal laws by the tax-exempt Federal Savings and Loan Insurance Corporation. The function of maintaining a liquidity fund is performed under Federal laws by the Federal home loan banks.

It is not maintained that the Savings & Loan Bank of the State of New York performs the function in New York of the FSLIC. It does not. It is noteworthy that approximately 90 percent of the members of the Savings & Loan Bank have insurance with the FSLIC. It is submitted, however, that the Savings & Loan Bank does perform the function in New York of the Federal home loan banks.

Section 13 of the Federal Home Loan Bank Act (12 U.S.C. 1433) exempts from State and Federal income tax the Federal home loan banks. This amendment to H.R. 3297 will provide equality for a State-chartered institution which is performing the same function as the Federal Home Loan Bank of New York. There is no reason to require that the Savings & Loan Bank of the State of New York perform the same functions as both the Federal Home Loan Bank of New York and the Federal Savings and Loan Insurance Corporation to receive tax exemption when Congress has split these functions between instrumentalities and granted exemptions from income tax to each.

We point with pride to the fact that New York has a strong dual banking system. Federal and State savings and loan institutions have been able to live side by side in the promotion of the financial stability and the general economic health of the State of New York and the Nation. Unless it is the intention of Congress to eliminate the "competition" of the Savings & Loan Bank of the State of New York, there is no justification for taxing the quasi-governmental instrumentality of the State of New York and exempting from tax the Federal Home Bank of New York.

The Savings & Loan Bank could be declared an instrumentality of the State of New York. By Federal definition, however, to be exempt from tax as an instrumentality of the State the assets of the Savings & Loan Bank would have to be wholly owned by the State, and all operating income would have to accrue to the State. It is not doubted that the Federal home loan banks are instrumentalities of the Federal Government. Yet, its assets are not owned by the Federal Government but are owned by the member associations, exactly the way the assets of the Savings & Loan Bank are owned. Neither does the income of the Federal home loan banks accrue to the Federal Government but rather, as in the case of the Savings & Loan Bank, to the member institutions that wholly own each bank.

The amendment to H.R. 3297 which I am here supporting will grant Federal tax relief for the Savings & Loan Bank similar to that enjoyed by its Federal counterpart in New York. While the Saving & Loan Bank of the State of New York has been in existence nearly 50 years, only for the past 2 years has the bank been subject to tax. The revenue which will be lost by this amendment by the Federal Government is de minimis; the loss of the Savings & Loan Bank of the State of New York to its member institutions and to the financial stability of the dual banking system in New York might well be catastrophic.

In asserting the similarity between the Federal Home Loan Bank of New York and the Savings & Loan Bank of the State of New York, the following additional facts are submitted to support our contention:

(*a*) The functions performed by the Savings & Loan Bank of the State of New York and the services authorized and rendered to its members are substantially the same as those of the Federal Home Loan Bank of New York. The powers and authority of the savings and loan bank have been prescribed by statutory provisions enacted by the Legislature of the State of New York and are set forth in the New York State banking laws. Likewise, substantially the same powers and authority have been conferred by the Congress of the United States upon the Federal Home Loan Bank of New York, as set forth in the United States Code.

I am submitting for the record a comparison of the principal statutory provisions which demonstrate the close similarity.

(*b*) The Savings & Loan Bank of the State of New York is authorized to issue shares to its members and pay dividends thereon. These shares, however, are not capital stock but are like shares of savings and loan associations. The shareholders can require the bank to redeem such shares with proper notice as provided in section 439(3) of the New York banking law. In section 1426 of title 12 of the United States Code, the Federal home loan bank's capitalization is divided into shares of capital stock which "share in dividend distribution without preference." The shareholders can require the bank to retire such stock with proper notice as provided in subsection (i). The provisions in both articles are substantially identical.

(*c*) Both institutions are authorized and empowered to offer similar services to their respective members. The extent of similarity of such authorized services includes the entire spectrum of demand deposits, time deposits, loans, safekeeping of securities, and the use of each bank's data processing facilities which are available for the benefit of their respective member institutions. I am submitting for the record a comparison of the principal services of the two institutions. This again demonstrates the similarity of the two institutions.

It is respectfully submitted that the history of the Savings & Loan Bank of the State of New York and the facts I have just summarized clearly indicate that under present conditions the State-chartered savings and loan associations' central bank in the State of New York is subject to a different standard of qualification for Federal tax exemption when compared to the Federal Home Loan Bank of New York for substantially the same functions and services and that a grave injustice will be suffered by the Savings & Loan Bank of the

State of New York if the relief sought for in this amendment is not granted by the Congress.

I wish to express my appreciation, in behalf of the New York State savings and loan associations, for the privilege of presenting their views before this honorable committee.

(The appendixes referred to follow:)

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS

Savings and Loan Bank of the State of New York[1]	*Federal Home Loan Banks*[2]
1. MEMBERSHIP	
"Membership in the savings and loan bank shall be limited to savings and loan associations, except, that the directors of the savings and loan bank may, in their discretion, permit federal savings and loan associations located in this state to be or become members of the savings and loan bank. * * *" (sec. 439(1)).	"Any building and loan association, savings and loan association, cooperative bank, homestead association, insurance company, or savings bank shall be eligible to become a member of, or a nonmember borrower of, a Federal Home Loan Bank if such institution (1) is duly organized under the laws of any State or of the United States; (2) is subject to inspection and regulation under the banking laws, or under similar laws, of the State or of the United States; and (3) makes such home mortgage loans as, in the judgment of the board, are long-term loans (and in the case of a savings bank if, in the judgment of the board, its time deposits, as defined in section 461 of this title, warrant its making such loans). * * *" (sec. 1424(a)).
"The incorporators shall subscribe and acknowledge and submit to the superintendent at his office proposed bylaws in duplicate, which shall prescribe the manner in which the business of such savings and loan bank shall be conducted with reference to the following matters: * * * 6. The minimum amount of shares necessary to qualify for membership. * * *" (sec. 433).	
NOTE.—The Legislature of the State of New York has delegated to the superintendent of banks the power to approve or disapprove the savings and loan bank's bylaws and amendments thereto:	
"The by-laws may be altered or amended, from time to time, provided such alterations or amendments shall have first received written approval of the superintendent and shall thereafter have been duly adopted at a meeting of the directors" (sec. 443).	
The present bylaws, therefore, are as binding on the savings and loan bank as the statutory provisions. Many of the present bylaw provisions correspond to the present statutory provi-	

[1] Cites are to art. 10-B of the New York banking law, as amended.
[2] Cites are to title 12 of the United States Code, as amended.

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*

1. MEMBERSHIP—continued

sions governing the Federal home loan banks.

"Any savings and loan association eligible for membership pursuant to Paragraph 1 of Section 439 of the Banking Law may become a member of the Savings and Loan Bank of the State of New York by the purchase from it of shares in an amount not less than one-half of one per centum of the association's own share liability as of December 31, 1947, or if thereafter organized as of the date of organization, but not less than five shares. Thereafter, the Board of Directors may, in its discretion, adjust the shareholding requirements of each member upon the basis of the Board's determined percentage of each association's share liability as of December 31st of any given year: *Provided, however*, That the determined percentage shall be uniform to all members except that no member shall hold less than five shares". (By-laws, art. I, sec. 1).

"The original stock subscription of each institution eligible to become a member under section 1424 of this title shall be an amount equal to 1 per centum of the subscriber's aggregate unpaid loan principal, but not less than $500. The bank shall annually, as of the close of the calendar year, adjust, at such time and in such manner and upon such terms and conditions as the Federal Home Loan Bank Board may by regulations or otherwise prescribe, the amount of stock held by each member so that such member shall have invested in the stock of the Federal Home Loan Bank at least an amount calculated in the manner provided in the next preceding sentence (but not less than $500). If the bank finds that the investment of any member in stock is greater than that required under this subsection it may, unless prohibited by said Board or by the provisions of paragraph (2) of this subsection, in its discretion and upon application of such member retire the stock of such member in excess of the amount so required. Said Board, in its discretion, may, by regulations or otherwise, provide for adjustments in amounts of stock to be issued or retired in order that stock may be issued or retired only in entire shares" (sec. 1426(c)(1)).

2. WITHDRAWAL FROM MEMBERSHIP

"Shares shall not be transferable, except that a member, which is not liable to the savings and loan bank for any direct obligation may transfer its shares therein to another savings and loan association, by and with the consent of the board of directors of the savings and loan bank; or it may retire from membership and receive back such sums as it has paid for its shares, upon giving one year's notice in writing to the savings and loan bank of such intention: *Provided, however*, That no withdrawal shall be permitted by the board of directors, which shall reduce the total amount of the capital of the savings and loan bank below five hundred thousand dollars. The board of directors may, in their discretion, waive such notice, in the event of the liquidation of any member, and pay back such sums as it has paid for its shares even though such payment should result in a reduction of capital below five hundred

"Any member other than a Federal savings and loan association may withdraw from membership in a Federal Home Loan Bank six months after filing with the board written notice of intention so to do, * * * [T]he indebtedness of such member or nonmember borrower to the Federal Home Loan Bank shall be liquidated, and the capital stock in the Federal Home Loan Bank owned by such member shall be surrendered and canceled. Upon the liquidation of such indebtedness such member or nonmember borrower shall be entitled to the return of its collateral, and, upon surrender and cancellation of such capital stock, the member shall receive a sum equal to its cash paid subscriptions for the capital stock surrendered, except that if at any time the board finds that the paid-in capital of a Federal Home Loan Bank is or is likely to be impaired as a result of losses in or depreciation of the assets

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*

2. WITHDRAWAL FROM MEMBERSHIP—continued

thousand dollars. Any member liable to the savings and loan bank for any direct obligation which holds shares in excess of the number required by the bylaws of the savings and loan bank, may transfer such excess shares to another savings and loan association, by and with the consent of the board of directors of the savings and loan bank; or it may, by and with the consent of the board of directors of the savings and loan bank, withdraw such excess shares and receive back such sum as it has paid for such excess shares, upon giving one year's notice in writing to the savings and loan bank of such intention: *Provided, however,* That no withdrawal of shares shall be permitted by the board of directors, which shall reduce the total amount of the capital of the savings and loan bank below five hundred thousand dollars" (sec. 439(3)).

held, the Federal Home Loan Bank shall on the order of the board withhold from the amount to be paid in retirement of the stock a pro rata share of the amount of such impairment as determined by the board" (sec. 1426(i)).

3. TRANSFER OF SHARES

"The incorporators shall subscribe and acknowledge and submit to the superintendent at his office proposed bylaws in duplicate, which shall prescribe the manner in which the business of such savings and loan bank shall be conducted with reference to the following matters: * * * 9. The transfer of membership, subject to the limitations of section four hundred thirty-nine of this article" (sec. 433).

"Shares shall not be transferable, except that a member, which is not liable to the savings and loan bank for any direct obligation may transfer its shares therein to another savings and loan association, by and with the consent of the board of directors of the savings and loan bank; * * *" (sec. 439(3)).

"Stock subscribed for otherwise than by the United States, and the right to the proceeds thereof, shall not be transferred or hypothecated except as hereinafter provided and the certificates therefor shall so state" (sec. 1426(h)).

"A Federal Home Loan Bank may, with the approval of the board, permit the disposal of stock to another member, or to an institution eligible to become a member, but only to enable such an institution to become a members" (sec. 1426(j)).

4. ADVANCES TO MEMBERS

"In addition to the powers conferred by the general corporation law the savings and loan bank shall, subject to the restrictions and limitations contained in this article and its by-laws, have the following powers: * * * 2. * * * to lend money to its members upon the security of their promissory notes with or without collateral" (sec. 435).

"Each Federal Home Loan Bank is authorized to make advances to its members upon the security of home mortgages, or obligations of the United States, or obligations fully guaranteed by the United States, subject to such regulations, restrictions, and limitations as the Board may prescribe. * * *" (sec. 1430(a)).

NOTE.—The Federal Home Loan Bank of New York makes available three types of advances: (1) Short-term advances, with a maturity of 1 year, repayable in equal quarterly installments; (2) long-term advances, with a maturity

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*
4. ADVANCES TO MEMBERS—continued	
	of over 1 year and up to 10 years, also repayable in equal quarterly installments; and (3) short-term 90-day advances. Short-term advances for a period of 1 year or less and 90-day advances may be granted on either an unsecured or a secured basis, at the option of the bank. All long-term advances must be collateralized.
5. DEPOSITS OF MEMBERS	
"The savings and loan bank shall not: 1. Do a general deposit business except with its members" (sec. 436).	"Each Federal Home Loan Bank shall have power to accept deposits made by members of such bank or by any other Federal Home Loan Bank or other instrumentality of the United States, upon such terms and conditions as the board may prescribe, but no Federal Home Loan Bank shall transact any banking or other business not authorized by this chapter" (sec. 1431 (e)).
6. SURPLUS ACCOUNT	
"The savings and loan bank shall accumulate from its profits a surplus account by carrying thereto annually a sum equal to one-half of one per centum of its capital, until such surplus account shall be equal to at least fifteen per centum of its capital" (sec. 438(1)).	"Each Federal Home Loan Bank shall carry to a reserve account semiannually 20 per centum of its net earnings until said reserve account shall show a credit balance equal to 100 per centum of the paid-in capital of such bank. After said reserve has reached 100 per centum of the paid-in capital of said bank, 5 per centum of its net earnings shall be added thereto semiannually. Whenever said reserve shall have been impaired below 100 per centum of the paid-in capital it shall be restored before any dividends are paid. Each Federal Home Loan Bank shall establish such additional reserves and/or make such chargeoffs on account of depreciation or impairment of its assets as the board shall require from time to time. No dividends shall be paid except out of net earnings remaining after all reserves and chargeoffs required under this chapter have been provided for, and then only with the approval of the board. * * *" (sec. 1436).
7. DIVIDENDS	
"The Board may declare dividends to the shareholders out of net earnings as ascertained, periodically, as it may by resolution determine. The rate of dividend shall be uniform to all shareholders, but shares issued between dividend periods shall participate in the	"All stock of any Federal Home Loan Bank shall share in dividend distributions without preference" (sec. 1426 (k)).

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*
7. DIVIDENDS—continued	
next succeeding dividend only in proportion to the time elapsed since the issue of such shares" (Bylaws, art. VIII, sec. 4).	
8. POWERS	
a. General	
"In addition to the powers conferred by the general corporation law * * *" (sec. 435).	"Each such bank shall have all such incidental powers, not inconsistent with the provisions of this chapter, as are customary and usual in corporations generally" (sec. 1432).
b. Investment	
"In addition to the powers conferred by the general corporation law the savings and loan bank shall, subject to the restrictions and limitations contained in this article and its bylaws, have the following powers: * * * 3. To invest its capital and other funds in bonds secured by first mortgages on real estate situated within the territory in which its member savings and loan associations are authorized to make loans; and in securities in which investments are authorized to be made by savings banks" (sec. 435).	"Each Federal Home Loan Bank shall at all times have at least an amount equal to the current deposits received from its members invested in (1) obligations of the United States, (2) deposits in banks or trust companies, (3) advances with a maturity of not to exceed one year which are made to members or nonmember borrowers, upon such terms and conditions as the Board may prescribe, and (4) advances with a maturity of not to exceed one year which are made to members or nonmember borrowers whose creditor liabilities (not including advances from the Federal home loan bank) do not exceed 5 per centum of their net assets, and which may be made without the security of home mortgages or other security, upon such terms and conditions as the Board may prescribe" (sec. 1431(g)). "Such part of the assets of each Federal Home Loan Bank (except reserves and amounts provided for in subsection (g)) of this section as are not required for advances to members or nonmember borrowers, may be invested, to such extent as the bank may deem desirable and subject to such regulations, restrictions, and limitations as may be prescribed by the board, in obligations of the United States, in obligations of the Federal National Mortgage Association, and in such securities as fiduciary and trust funds may be invested in under the laws of the State in which the Federal Home Loan Bank is located" (sec. 1431(h)).
c. Borrowing	
"In addition to the powers conferred by the general corporation law the savings and loan bank shall, subject to the	"Each Federal Home Loan Bank shall have power, subject to rules and regulations prescribed by the board, to

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*

8. POWERS—continued

c. Borrowing—Continued

restrictions and limitations contained in this article and its bylaws, have the following powers: 1. To issue, sell, and redeem bonds and notes secured by bonds and first mortgages made to or held by its members and to issue, sell, and redeem debenture bonds and notes" (sec. 435).	borrow and give security therefor and to pay interest thereon, to issue debentures, bonds, or other obligations upon such terms and conditions as the board may approve, and to do all things necessary for carrying out the provisions of this chapter and all things incident thereto" (sec. 1431(a)).

d. Ownership of real estate

"In addition to the powers conferred by the general corporation law the general corporation law the savings and loan bank shall, subject to the restrictions and limitations contained in this article and its by-laws, have the following powers: * * * 5. To purchase in its own name, hold and convey real property for the following purposes and no others: (a) A plot whereon there is or may be erected a building suitable for the convenient transaction of its business from portions of which not required for its own use a revenue may be derived. "(b) Such as shall be mortgaged to it in good faith, by way of security for loans made by it or moneys due to it. "(c) Such as shall be conveyed to it for debts previously contracted in the course of its business, and such as it shall purchase at sales under judgments, decrees or mortgages held by it" (sec. 435). "The savings and loan bank shall not: * * * 3. Invest more than twenty-five per centum of the surplus account in real estate occupied, or to be occupied, by it as a place of business, without the written approval of the superintendent" (sec. 436).	"Upon the making and filing of such organization certificate with the board, such bank shall become, as of the date of the execution of its organization certificate, a body corporate, and as such and in its name as designated by the board it shall have power * * * to purchase or lease and hold or dispose of such real estate as may be necessary or convenient for the transaction of its business, but no bank building shall be bought or erected to house any such bank, nor shall any such bank make any lease for such purpose which has a term of more than ten years; * * *" (sec. 1432).

9. EXEMPTIONS

"The bonds and notes issued by the savings and loan bank and the savings and loan bank itself, together with its capital, accumulation and funds, shall have the same exemption from taxation as other institutions for savings. No law which taxes corporations in any form, or the shares thereof, or the accumulations therein, shall be deemed to include the savings and loan bank or its issues of bonds or notes unless they are specifically named in such law" (sec. 446).	"Any and all notes, debentures, bonds, and other such obligations issued by any bank, and consolidated Federal Home Loan Bank bonds and debentures, shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes; now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The bank, including its franchise, its capital, reserves, and surplus, its advances, and its income, shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency,

APPENDIX A. COMPARISON OF PRINCIPAL STATUTORY PROVISIONS—Continued

Savings and Loan Bank of the State of New York	*Federal Home Loan Banks*
9. EXEMPTIONS—continued	
	or possession thereof, or by any State, county, municipality, or local taxing authority; except that in any real property of the bank shall be subject to State, Territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed. The notes, debentures, and bonds issued by any bank, with unearned coupons attached, shall be accepted at par by such bank in payment of or as a credit against the obligation of any homeowner debtor of such bank" (sec. 1433).

APPENDIX B. COMPARISON OF PRINCIPAL SERVICES

Savings and Loan Bank of the State of New York	*Federal Home Loan Bank of New York*
1. Provides either secured or unsecured loans to members for short- or long-term needs.	1. Provides either secured or unsecured loans to members for short- or long-term needs.
2. Provides demand accounts for members for clearing and settlements.	2. Provides demand accounts for members for clearing and settlements.
3. Provides time accounts for members with cash reserves in excess of operating requirements.	3. Provides time accounts for members with cash reserves in excess of operating requirements.
4. Provides safekeeping of members' securities.	4. Provides safekeeping of members' securities.
5. Provides data processing services for members including mortgage and savings account servicing.	5. Provides data processing services for members, including reconcilment services for drafts, Christmas Club and dividend checks, and money orders.
6. Does not provide foreign draft and foreign payment order facilities.	6. Provides foreign draft and foreign payment order facilities.
7. Does not provide research and statistical information.	7. Provides research and statistical information.
Does not provide insurance of accounts of members.	Does not provide insurance of accounts of members.

The CHAIRMAN. Thank you.

How much of your income would not be taxed which is now taxed, of your members?

Mr. RABSTEJNEK. Senator Byrd, the point is we have not been taxed up until the time of our notice to revoke our exempt status. We have been subject to the tax for the first time in 1963, at which time we paid approximately $1,800 tax.

The CHAIRMAN. Approximately what?

Mr. RABSTEJNEK. $1,800, and it has not yet been finalized because the interpretations have not been clarified by the Internal Revenue Service. So far for 1964 they run $10,000.

The CHAIRMAN. In other words, you would save $10,000 by this amendment?

Mr. RABSTEJNEK. That is right, sir.

The CHAIRMAN. How many different organizations are there?

Mr. RABSTEJNEK. Of our type?

The CHAIRMAN. Yes.

Mr. RABSTEJNEK. We are the only one, sir; and the amendment provides that the exemption be granted only to those institutions that do perform a function similar to what the Federal Home Loan Bank provides, provided they were incorporated prior to the inception of the Federal Home Loan System for which we were the prototype, and we are the only institution of that type.

The CHAIRMAN. All right, sir. Thank you very much.

Mr. RABSTEJNEK. Thank you.

The CHAIRMAN. The committee will adjourn until 10 o'clock tomorrow morning in executive session to consider this and a number of other House-passed bills.

(Whereupon, at 12:10 p.m., the committee was recessed, to reconvene at 10 a.m., Wednesday, July 22, 1964.)

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