

NATIONAL MONETARY COMMISSION

State Banking Before the
Civil War

BY

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AND

The Safety Fund Banking
System in New York
1829-1866

BY

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University of Pennsylvania



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STATE BANKING BEFORE THE CIVIL WAR.

I. PAYING IN OF CAPITAL.

Beginning with the period of national independence the earliest banking experiments were founded on specie. The Bank of North America, 1781, was based on specie obtained by the Government from France; and the Bank of Massachusetts had collected in specie \$253,500, out of its total capital of \$300,000, before it began operation. There was, however, no great supply of precious metals in the country, and when banks began to increase in number it was found impossible to adhere to this conservative rule. Hamilton recognized that it would be impossible to found a great national bank on specie, and so, following the example of the Bank of England, in 1790 recommended the use of government securities. The charter of the First Bank of the United States accordingly provided that only \$2,000,000, or one-fourth of the capital subscribed by individuals, should be paid in gold and silver, and the remainder in government stock. Even for this comparatively small amount payment by installments was permitted, and the bank was authorized to begin operations when \$400,000 was paid in. This method was repeated in the capitalization of the Second United States Bank in 1816. In nearly all local charters provision was made that the State should subscribe for a portion of the capital, but

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this subscription did not necessarily mean that money was actually to be paid in, but rather stock or bonds. The United States Government, which subscribed for \$2,000,000 of the stock of the First Bank, borrowed its subscription from the bank. But the bank, having no money to lend, passed a credit of \$2,000,000 on its books to the Government, on which it paid 6 per cent.^a In the case of the Bank of Pennsylvania, 1793, the State subscribed for its third, or \$1,000,000, of the capital in United States stock, and again, in 1803, took advantage of this privilege when such securities were selling at a discount. The charter of the Bank of America in New York, 1811, with a capital of \$6,000,000, allowed \$5,000,000 to be subscribed in stock of the Bank of the United States and called for only \$1,000,000 in cash.

The instability of bank capital was rendered even more insecure by abuses of a flagrant character. As a rule, subscriptions were made in installments extending from one to four years, and it became a common practice for subscribers, after the first installment was paid, to pledge their stock, then only partially purchased, back to the bank for a loan with which to settle for subsequent obligations. "Speculators in shares were not slow to perceive that if they could put their own stock notes into the bank instead of cash, they might get something for nothing. If the bank survived the dividends would probably exceed the interest on the stock notes, the difference being a clear gain to the shareholders, without any investment of their

^a Gouge: *Inquiry into the Principles of the American Banking System*, p. 72.

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own money.”^a Many banks, therefore, were established on an inadequate specie basis, represented by a first installment of from 5 to 15 per cent of the capital. In 1820 Secretary Crawford reported that although the banking capital was nominally over \$125,000,000, including that of the Second United States Bank, the actual capital paid in was only \$94,000,000. The active capital, however, in his opinion, did not even reach this, as stockholders were allowed permanent accommodations at the bank or were permitted to pay portions of their stock subscriptions with their own notes. In this way most of the banks established after 1812 had been organized: “Not because there was capital seeking investment, not because the places where they were established had commerce and manufactures which required their fostering aid, but because men without active capital wanted the means of obtaining loans which their standing in the community would not command from banks or individuals having real capital and established credit.”^b The active capital was consequently estimated as not over \$75,000,000.

Gouge vividly describes the method: “The first installment, which we shall suppose to be \$5 on a share, enables the banks to purchase desks and the counter and to pay for engraving and printing its notes. It has, then, the necessary apparatus for commencing its operations, and it has, perhaps, a specie fund in reserve, of three or four dollars for each share of stock, to meet contingencies. It then begins to discount notes and circulate paper. As

^a White: *Money and Banking*, p. 291.

^b Report of the Secretary of the Treasury, February 24, 1820.

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the bank notes will serve the purposes of trade in the neighborhood, the specie is sent to distant places to procure commodities. Then comes the time for paying the second, third, or fourth installment. The bank makes a call on the stockholders. Some of them hypothecate their stock; that is, pledge it to the bank and with the means obtained from the bank itself pay in their proportion. Others have obtained the means by discounts of accommodation notes without any hypothecation of stock. Some few pay in real money, but they generally pay in the notes of the bank itself, or of similar institutions. Thus, bank capitals are formed by exchanging one kind of promises to pay for another kind of promises to pay. This mode of forming bank capitals with the stock notes of the subscribers is not peculiar to banks of the second and third order. The banks of the most approved standing have formed their capitals in the same way.”^a Under the conditions of the charter of the First United States Bank it is not probable that more than \$500,000 of a total of \$10,000,000 was ever paid in specie. This method was repeated in the establishment of the Second Bank, for the third installment was not paid in specie, but in bank notes or stock notes. Lowndes, of South Carolina, in a congressional debate in 1818, declared that everyone anticipated the payment of the capital of this bank by notes discounted for that purpose; as the bank was in full operation it could not be expected to exclude its own stockholders from discounts; and it was probable that a

^a Gouge: Inquiry into the Principles of the American Banking System, pp. 71-72.

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bank had never gone into operation in which the same thing had not occurred.^a

In Massachusetts the policy was variable, "showing that some people could get inserted in bank charters privileges which others could not get."^b The charter of the Nantucket Bank, 1795, provided that no stockholder could borrow at the bank until he should have paid his full proportion of each installment as it became due. This did not, as White points out, prevent the subscriber from borrowing the money after it had been paid in. "In the following year the Merrimac Bank of Newburyport was chartered with a capital stock of not less than \$70,000 nor more than \$150,000. Here we find an attempt to evade the principle affirmed in the charter of the Nantucket Bank. No loans were to be made to shareholders until they had paid their proportion of \$70,000. If they should choose to have a capital of \$150,000, they might borrow from the bank itself all except the first \$70,000. There was much contrariety of legislation until 1804, when several charters contained an express provision that no money should be loaned to anybody until satisfactory evidence was presented to the governor and council 'that the whole capital stock aforesaid is actually paid in and existing in gold, silver, or other metals in their vaults.' Even this provision was not sufficient, for it was proved in more than one case that banks borrowed the entire amount of their capital in gold and silver coin from other banks and, having exhibited it to the bank officials, re-

^a Annals of Congress, 15th Cong., 2d sess., I : 329.

^b White: Money and Banking, p. 291.

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turned it to the rightful owners on the same day. Accordingly, in 1811, a clause was inserted in bank charters requiring the directors to take an oath that the money paid in was intended to remain there as the capital of the bank,"^a and by the charter of the State Bank, 1811, the bank was not to begin operations until one-fifth of the capital had been paid in gold and silver and examinations had been made by the commissioners. Later the proportion was raised to one-fourth.^b In 1813 it was enacted that three commissioners should be appointed by the governor to count the gold and silver and to take the oaths of the directors that it had been paid in *bona fide* by the stockholders as the bank's capital and for no other purpose, and that it was intended to remain there, and in 1822 it was enacted that no dividends should be declared until the whole capital was paid in. As evidence of the criticism which was aroused at an early date, the following resolutions, which were laid before the house of representatives in Massachusetts in 1804, may be cited:

"Resolved as the opinion of this house, That in future the incorporation of any bank ought to be granted, but with the following restrictions:

"First. No bank to commence discounts until one year after an act shall have been passed for that purpose.

"Second. No bank to commence discounts until evidence shall have been given that the whole of the capital shall have been paid in and is actually existing in specie in the vaults.

^a White: Money and Banking, pp. 291-292.

^b Commonwealth Bank, 1824.

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“Third. That evidence shall be produced that the entire capital in specie in any bank has been imported from foreign countries after its incorporation and before its operation.”

Although Massachusetts through its legislation sought to attain a high standard, there are abundant illustrations of the loose practices which prevailed. In 1819, a legislative committee of Massachusetts reported that at the organization of the Agricultural Bank in Pittsfield, the first installment, \$45,000, was placed in the vaults, with the expectation that it would be repaid by a loan to stockholders. The next day \$32,000 was taken back as a loan for which notes without indorsers were given and on shares pledged as security.^a During the speculative period which culminated in 1837, the law was openly evaded. The City Bank in Lowell under its charter was to receive one-half of its capital, or \$75,000, in specie; \$43,000 of this, however, was obtained from Boston banks on agreement that it should be returned, and \$20,000 was obtained from Lowell banks on the same condition. The balance of the capital was paid in checks, but no one could tell on what bank the checks were drawn and not one of them was ever paid or presented for payment.^b Again in 1838 the Bank Commissioners reported that the North Bank of Boston had for many years been in the habit of buying up its own stock at auction and selling it in advance, and it was held an idle ceremony to require a full amount of stock to be paid in within a given period, if, on the next day, it might rightfully be

^a Resolves, 1819, ch. 245.

^b Report of Bank Commissioners, Massachusetts, 1837.

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purchased back again from the stockholders and yet the institution go on as a legal banking corporation, without stockholders and without stock. It was also noted that, notwithstanding the explicit provisions of law, some argued that the giving of a note of hand or a memorandum check secured by pledge of shares, was a substantial compliance with the law. To such violations and evasions were attributed most of the bank failures which occurred in Massachusetts.^a

In Rhode Island the charter of the Providence Bank, 1791, provided for the payment of two-fifths in specie and the balance in United States stock.^b Before many years, however, the requirement that stock be partly or wholly paid in specie was frequently omitted and the payment of a later installment was deferred. For the period, 1800-1860, it has been estimated that not more than one-third and possibly not more than one-fifth of the nominal capital of all the banks in that state was paid for in any other way than stock notes. In the case of the Farmers' Exchange Bank of Gloucester, 1804, a cash deposit of only one dollar per annum was required with the subscription, and remaining payments were extended over three years.^c In 1826 a legislative committee opposed the grant of new charters chiefly on the ground that banks were founded on an artificial basis. Although the charters usually provided that capital should be paid in specie, evasions were the rule. The specie paid in one day, frequently borrowed for the purpose, was withdrawn the next day, and the notes of stockholders

^a Report of Bank Commissioners, Massachusetts, 1838.

^b Stokes: *Chartered Banking in Rhode Island*, p. 9.

^c *Ibid.*, p. 17.

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were substituted. At the payment of each successive installment, the process was repeated. Said the chairman of the committee: "The notes given for the stock and the stock pledged for the notes, cancel and annul each other; or rather they are both nullities from the beginning. * * * That by far too great a portion of the capital of the banks already granted consists of nothing better than such notes is to be inferred from their reports, by which it appears that nearly \$1,500,000 is due them from their stockholders."^a Although there was a temporary check given to organization, abuses continued. In the charter of the Arcade Bank in Rhode Island, 1831, more than a year was given to pay by installments. In 1836 the Massachusetts method was adopted: no bank could go into operation until one-half of the capital was paid in, to the satisfaction of the bank commissioners, certified to under oath; and the remainder was to be paid in within one year under penalty of forfeiture of the charter.^b

The same laxness existed in Connecticut. The charter of the Hartford Bank, 1792, called for initial payments of only 35 per cent, and the historian of that institution writes that it was reasonable to conjecture that at the outset the assets of the bank consisted of the promissory notes of the stockholders, indorsed by each other, with a sprinkling of gold drawn from old hoards and possibly a few notes from the Bank of North America.^c The charter of the Farmers' and Mechanics' Bank, Hartford, 1833,

^a Stokes: *Chartered Banking in Rhode Island*, pp. 33-34.

^b Report of Bank Commissioners, Rhode Island, 1836.

^c Woodward: *The Hartford Bank*, p. 6.

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provided for payment in specie, or notes of Connecticut banks or the Bank of the United States or of the City of New York, provided the notes were at par in Connecticut, in installments up to 30 per cent, and the residue at such times as the directors should determine. In 1852 the general banking law required that one-half of the capital be paid in before beginning operations, and the remainder within a year.

In the formation of the Bank of Maine in 1812, after the payment of one-fourth of the capital (\$37,500 out of \$150,000), large loans were made to stockholders. It was afterwards shown that within a year discounts to stockholders on pledge of stock amounted to \$137,750.^a Bank returns for the whole State in 1814 showed that four-ninths of the capital was made up of stockholders' promises secured by real estate and bank stock.^b Gradually there was improvement. In 1831 the general banking law forbade the use of stock notes. In 1837 the bank commissioners reported that in some instances loans had been made to stockholders before capital had been paid in, but this departure from sound methods was attributed to inadvertence rather than to deliberate intention.^c

In New Hampshire it was common to require the payment of capital in specie, but the stockholders determined the amounts of payment and the times when they should be made. In 1838 the bank commissioners complained that stock notes were frequently received. In Vermont the earlier charters, as in that of the Bank of Burlington,

^a Report of Committee, p. 5.

^b Knox: History of Banking in the United States, p. 330.

^c Report of Bank Commissioners, Maine, 1837.

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1818, permitted the directors to determine how much should be paid in. In 1831 the payment of one-half, to be certified to on oath, was required; and in 1840 it was enacted that one-half was to be paid in specie and the remainder within two years.

In New York, the charter provisions dealing with the paying in of capital were very lax. For example, the charter of the Mechanics Bank, 1810, permitted directors to call for payments from the stockholders in such proportions as they saw fit. No transfer of stock, however, could be made until one-half had been paid in. In 1818 a committee of the New York legislature reported that the major portion of the circulation of the State had been issued by banks whose nominal capitals were small and composed largely of notes of stockholders, called stock notes.^a In many cases but a small proportion of the authorized capital was paid in, even through stock notes. For example, the Greene County Bank in 1820 had only \$44,000 of a subscribed capital of \$90,000 paid in; the Washington and Warren Company, with subscribed capital of \$400,000, had \$176,218 paid in; the Bank of Geneva, with a subscribed capital of \$400,000, had \$100,000 paid in; in 1824 the Central Bank, with a subscribed capital of \$200,000, had but \$45,000 paid in; and the Bank of Plattsburgh, with a subscribed capital of \$300,000, had but \$60,000 paid in. In two charters granted in 1825 a step toward conservatism was taken in a requirement that 50 per cent of the capital be paid in.^b Payment in specie, however, was not enforced; and a legislative committee

^a Niles, 14:39; New York Assembly Journal, 1818, p. 309.

^b Session Laws, New York, 1825, ch. 117.

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in 1826 reported that it was well known that the capital of banks chartered for several years had been paid in with the bills of institutions previously chartered (Jan. 16, 1826). In the Safety Fund Act of 1829 the payment of the whole capital was required. In 1835 it was reported that more than usual of the bank capital during the previous year had been paid in only to be borrowed by the stockholders under pledge of stock. The bank commissioners, therefore, suggested that the hypothecation of stocks should for a certain length of time be prohibited.

In New Jersey, a general law of 1812 provided that the several installments should be paid as the directors might designate,^a and this easy method was continued throughout the period of state banking until 1863. Occasionally, there was a requirement that one-fifth, one-fourth, or even one-third of the capital should be paid in at the beginning of operations.^b Charters also provided, as in 1815, for payments in gold, silver, or bank notes of equal value; in 1816, for payment, one-fifth in government stock, and the balance in specie or bank notes;^c and in 1828, in specie, notes of the Bank of the United States, or notes of specie paying banks in New Jersey and New York City.^d

Pennsylvania by its act of March 21, 1814, chartering 41 banks, provided that when one-half of the shares were subscribed for and 20 per cent of the par value paid in, the banks would receive full corporate powers. By the general banking act of 1824, it was provided that \$5 on a par value of \$50 should be paid in at the time of subscrip-

^a Laws, New Jersey, 36 Assembly, 2 sess., pt. 5, sec. 4.

^b Private acts, New Jersey, 1815, 39 Assembly, 2 sess., 32.

^c Private acts, New Jersey, 1816, 40 Assembly, 2 sess., 48.

^d Acts, New Jersey, 52 Assembly, 2 sess., 131, sec. 6.

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tion, and the remainder as soon as the bank was organized and the officers chosen. The bank was to receive a certificate, however, from the commissioners when one-fifth of the capital had been paid in. Here again, there was no absolute assurance that the capital was in money. Investigation in 1842, of the Girard Bank, showed that the increased capital obtained in 1836 was received by accepting notes, which in some cases were renewed indefinitely.

In Maryland, up to 1810, there is no evidence of the use of stock notes^a but the requirements of payment in specie varied. The Bank of Maryland, 1790, with a capital of \$300,000, had \$200,000 paid in foreign gold coin before it commenced business,^b but subsequent charters generally required only one-fourth of the capital to be thus met. By the charter of the Union Bank, Maryland, 1805, no dividend was to be distributed until \$50 on \$100 of stock had been paid in, and installments were extended over five years. Between 1810 and 1818, the use of stock notes became common. A part of the capital, usually about one-third, was required to be paid in gold or silver, or the notes of specie paying banks, but no provision through state supervision provided for obedience to the law.^c The country banks thus established were consequently weak, particularly in periods of monetary pressure. Moreover, the use of installments and stock notes tended to attract an unsubstantial and speculative class of stockholders; "if the bank fared well, the stockholder enjoyed dividends on the whole amount of the

^a Bryan, *History of State Banking in Maryland*, pp. 32, 34.

^b *Ibid.*, p. 20.

^c *Ibid.*, p. 65.

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stock; if it failed, he could absolve his indebtedness to it by paying in his certificates of stock. Thus he had all to gain and was irresponsible for losses."^a In 1840, a legislative committee reported that several of the banks incorporated since 1834 received their capital through loans to stockholders.

In Virginia the installments were called for more promptly; the final payments of the capital of the bank of Alexandria, 1792, being due in six months.^b Only one-tenth was required in specie at the initial subscription. The charter of the Farmers' Bank of Virginia, 1812, however, required that all installments be paid in gold or silver coin;^c while the Bank of Northwestern Virginia, 1817, had to have three-fifths of its capital paid in current coin before it began operation,^d and this was restated in the general act of 1837. In 1850, the proportion was reduced from three-fifths to one-half.^e

In North Carolina the charters of the first two banks, organized in 1804, directed that the capital be paid in gold or silver, but each of them could begin business after one-tenth of the capital was paid in. In 1810 the charter of the State Bank provided that three-fourths only of each share should be paid in specie, and the remaining fourth in paper currency, if desired. It was afterward stated that the first two installments were paid in gold and silver and the remainder in bank notes. In the extension of the first two charters in 1814, all reference

^a Bryan, *History of State Banking in Maryland*, p. 66.

^b Hening, *Statutes at Large*, ch. 77, sec. 2.

^c Acts of Virginia, 1812, Pt. vii, sec. 3.

^d Laws, Virginia, 1817, ch. 39, sec. 5.

^e Laws, Virginia, 1849-50, ch. 57.

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to subscription in specie is omitted, and the capital was largely paid in stock notes.^a

By the charter of the Planters' and Mechanics' Bank at Huntsville, Ala., 1816, permission was given to begin business when one-tenth of the capital was subscribed; one-eighth was to be paid in at the time of subscription, three-eighths as soon as the bank began operations, and the remaining one-half in two equal installments at periods of sixty and one hundred and twenty days. The constitution of 1819 provided that no bank could begin operations until half the capital stock was actually paid in, in gold or silver, and that this amount in no case could be less than \$100,000. In Mississippi, the bank commissioners in 1838 reported that the stock of practically every bank in Mississippi had been paid in notes of individuals and mortgages on property. Charters gave an opportunity for this, in using the words, "secured to be paid." The issues of a bank were consequently not based upon what the stockholders had paid into the bank, but on what they owed to the bank, thus making their indebtedness and not their actual capital, the basis of their circulation.

The charter of the Bank of Florida, 1828, which did not, however, go into operation, gave the bank the privilege to begin business when \$40,000 out of a capital of \$500,000 had been paid in, in gold or silver or notes of the United States Bank. The charter of the Bank of Pensacola, 1831, providing for a capital of \$200,000 authorized the

^a See Report of Legislative Committee of Investigation, North Carolina, 1828-29; Sumner, *History of Banking*, 1:45.

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institution to open when \$15,000 had been paid in, three-fourths in gold, silver, or United States bank notes, and one-fourth in current money. Within a few months the charter was amended so as to permit it to begin operations when \$7,000 had been paid in.^a The constitution adopted in 1845 required that capitals should be paid in specie. The borrowing of money to create or to add to capital and the making of loans on pledge of stock were forbidden.

The charter of the Bank of Orleans, Louisiana, 1811, admitted subscriptions payable in money or "notes payable to the directors." According to Sumner^b this charter and that of the Louisiana State Bank, 1818, are the only two acts of incorporation he found which contained explicit provision for what appeared to be stock notes. In 1833, a term of three years was allowed to the stockholders of the Commercial Bank of New Orleans for the payment of capital.

In Ohio, the charter of the Bank of Muskingum, 1812, prohibited the payment of dividends to stockholders until they had paid in all their stock; the charter of the Bank of Hamilton in 1818, provided that the capital should be paid up in "money of the United States;" the charter of the Bank of Gallipolis provided that the Government should send a commissioner to see that \$20,000 of its authorized capital of \$300,000 was actually in hand, one-half in specie and one-half in United States bank notes, before the bank should open.^c Later in 1833, the Frank-

^a Act of February 6, 1832.

^b History of Banking, 1:61.

^c Sumner, History of Banking, 1:92.

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lin Bank of Cincinnati was authorized to begin business when one-fourth of the capital had been paid in specie, and after examination by the commissioner appointed by the governor, who had power to take the oaths of the officers. The capital was to be paid in installments, \$10 down and the remainder in varying sums within periods not extending over six months.

A Kentucky act, January 26, 1818, which authorized the incorporation of a large number of new banks, provided that capital could be paid in current money, notes of the Bank of the United States or of the Bank of Kentucky. The payment of the last three installments could be deferred and the bank could open when one-fifth of the capital had been paid in. The requirements of the Louisville Bank charter, 1833, were practically identical with those of the Franklin Bank in Ohio. Promptness in securing the payment of installments was not enforced; the Northern Bank of Kentucky in Lexington, organized in 1835, reported two and a half years later, that but 80 per cent of its capital had been paid in and that its calls for stock had been as rapid as was usual in other banking institutions. In Tennessee, it was impossible from the books of the Union Bank, 1837, to show the kinds of funds in which the stockholder paid for stock. It was believed, however, that it consisted of specie, notes on specie-paying banks, and checks on the bank.

In the charter of the State Bank of Indiana, 1834, it was provided that before commencement of business, one-half, or \$80,000 of the capital of each bank, must be paid in specie, \$30,000 by individuals, and \$50,000 by the

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State. The balance was to be paid in two equal installments, in specie. Individual subscribers could borrow from the State for paying their second and third installments upon mortgages of real estate, and for this purpose, the State was to sell bonds to the amount of \$1,300,000.^a The charter of the Bank of the State of Indiana, 1855, called for \$2 down on each share of \$50, and the balance by such installments as the directors might require.^b

In Illinois, the early charters required but little solid capital. The Bank of Illinois at Shawneetown prescribed but \$10 in specie on each share and the remainder at the call of the directors; for the Bank of Edwardsville, 1818, but \$5 in specie or bank bills "which will command the same," was demanded. The charter of the Bank of St. Louis, 1813, provided that the installments should be paid in gold or silver or in good approved paper of the banks of Kentucky, the State Bank of Tennessee, the banks of Cincinnati, Vincennes, and Richmond, or such other bank paper as is received by the United States in payment for lands and taxes.^c

II. DISTRIBUTION OF STOCK.

Influenced by a fear that banks might concentrate the money power in the hands of a few, some of the States inserted elaborate provisions in the charters providing that the initial subscription be opened in different parts of the State, and limiting the number of shares which could be taken by any one, person. This restriction, however,

^a Laws, Indiana, 1834, ch. 7, sec. 90.

^b Laws, Indiana, 1855, ch. 111, sec. 81.

^c Missouri Gazette, October 5, 1816.

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was of little service, as shares were taken out by attorney. Congress in chartering the first United States Bank expressly required that the subscription books should not be opened for several months (until July 1) in order to allow citizens in different parts of the country to prepare to subscribe, and thus, if possible, lessen the control which might otherwise have fallen into the hands of citizens of Philadelphia and near-by cities.^a Moreover, for three months after July 4 no one could subscribe on any one day for more than 30 shares. Notwithstanding these restrictions, there was severe criticism of the commissioners on the ground that they were partial in the distribution, and thus aided the speculation in shares, which immediately took place.

In Connecticut the charter of the Hartford Bank, 1792, forbade anyone save the State to own more than 30 of the 250 shares, but in 1796 this restriction was removed so as to provide for an increase of capital.^b Much regret was later expressed that ownership of stock too frequently drifted into the hands of non-residents, and bank officials were called upon to report in regard to ownership, as: How much was owned in the town where the bank was located, how much in other towns in the county, in other counties in the State, and out of the State.^c From such a return, it was shown that out of 5,000 shares of the City Bank of New Haven 2,470 were taken by residents, and 2,530, or more than a majority, outside. In 1836, Rhode

^a Supplementary bill, March 20, 1791.

^b Woodward: *The Hartford Bank*, pp. 17, 75.

^c Report of Bank Commissioners, Connecticut, 1837, p. 7.

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Island, in a general banking act, enacted that commissioners should take charge of subscriptions and that in the allotment of stock the inhabitants of the town in which the bank was located should have preference, to be followed by those residing in towns of the same county. In 1850 it was provided that the commissioners appointed by the governor should apportion the stock "as near as may be to the amount subscribed by each person who shall in their opinion have the ability and disposition to make a bona fide investment." Most subsequent charters had a like provision. By the charter of the Commonwealth Bank of Massachusetts, 1824, original subscribers were prohibited from selling or transferring their stock for one year after organization, and in 1831 the legislature prohibited any individual or corporation from holding more than 50 per cent of the capital of any bank, except such as might be held as collateral security.

Beginning with about 1840 bank commissioners in New England States frequently complained of the efforts made by outsiders, particularly residents of New York, to obtain control of banks for the purpose of securing accommodation and circulating the bank bills in other States. These speculators then sought to buy up these bills at a discount for the purpose of again loaning them.^a A special advantage was gained if these notes could be sent to a distance in the West.^b In 1841 the bank commissioners of Maine stated as a cause for criticism that more

^a The Roxbury Bank, Massachusetts, failed in 1838, due, it was stated, to the speculative operations of New Yorkers who owned the stock *Financial Register*, 2:142.

^b Reports of Bank Commissioners of Vermont and Maine, 1841.

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than \$500,000 of bank stock was owned outside the State, in part due to the desire to evade taxation;^a and in the same year the governor of New Hampshire recommended legislation to prevent the control of a bank passing into the hands of non-residents. As late as 1859 complaint was made of the extraordinary efforts of outside speculators, principally of New York, to obtain control of some of the smaller banks. The commissioners of Massachusetts joined in these criticisms and declared that non-resident control had proved ruinous in nearly every case.^b

In New York there were few, if any, limitations on the residence of stockholders. In the organization of the Mechanics' Bank in New York City, 1810, the General Society of Mechanics and Tradesmen was permitted to subscribe for one-tenth of the capital, while four-tenths was reserved for mechanics and tradesmen of the State. Charters in 1811 provided for the appointment of special commissioners who should supervise the distribution of the stock, and this method was subsequently continued.^c This, in turn, gave rise to a new form of corruption, as in the organization of the Commercial Bank of Albany, 1825, when the commissioners appointed by the legislature appropriated to themselves and a few favorites the majority of the shares.^d Another notable illustration of political intrigue is found in the assignment of the stock of the Seventh Ward Bank of New York City, 1832; for a capital of \$500,000 more than the \$6,000,000 was

^a See also Report of 1859.

^b Report of Bank Commissioners, Massachusetts, February, 1841.

^c Session Laws, New York, 1811, ch. 68; 1824, ch. 46.

^d Albany Argus, June 14, 1825.

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subscribed; of the 3,710 shares assigned, 1,135 were distributed to family connections of the commissioners and the remaining 2,535 were apportioned among public officials, leaving only 40 to outside subscribers.^a In 1829 it was complained that a large part of the bank capital in the State had been furnished by non-residents and foreigners.^b Much criticism was aroused because of the foreign ownership of the Manhattan Bank in New York City, whose stock was largely owned by the Marquis Camarthaen. In 1832 the bank commissioners reported that too many banks were organized, particularly in the country, because of the demand for such investments by non-residents rather than because of any redundancy of capital in the immediate neighborhood. "When men of capital abroad were found willing to make such investments at a trifling premium, competition became animated and enormous subscriptions were made for the purpose of realizing a premium upon the sale of bank stock."^c Many applications originated with individuals who desired to realize the first profits upon the stock which was to be created; the same persons were found petitioning for a number of institutions in different parts of the State; and there were many contests as to who should be the commissioners to distribute the stock.^d The governor of the State suggested that bank stock be sold at public sale so that the premium should go to the

^a Niles, 44:371; Senate Document, New York, No. 47, February 4, 1834; Senate Documents, Nos. 64, 73, 89, 94.

^b Senate Report, New York, January 19, 1829.

^c Report of the Bank Commissioners, New York, 1832.

^d See also, Senate Document, New York, No. 108, March 25, 1834; Senate Document, No. 58, April 1, 1837.

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State instead of to speculative subscribers. On the other hand, it was claimed that this would facilitate the concentration of the stock in the hands of a few wealthy persons and throw the bank into the hands of individuals at a distance from its location who would use its facilities for private purposes rather than for the accommodation of local customers.^a Again, in 1837, the bank commissioners stated that the method of distribution of bank stocks was very unsatisfactory. There were violent contentions and bitter personal animosities; funds were frequently advanced by other banks to those who wished to buy stock in a new bank, thus substantially repeating the old stock-note system. Although it was difficult to devise a satisfactory plan for parceling out a franchise possessing a pecuniary value, the commissioners suggested that an individual should be limited as to the number of shares; that shares should not be transferable for thirty days; that subscribers should take oath that they had paid in with their own money and had not pledged or hypothecated the stock in any way, or held it in trust in secret. In the same year a law was passed providing for the sale of bank stocks at auction whenever new capital was created. In 1854 the superintendent of the bank department reported that the only failures of banks in the previous eight years by which bill holders had suffered a loss had been those located in remote parts of the State owned by brokers and speculators residing in other sections.^b

In New Jersey, by a charter of 1824, citizens of the State were to have a prior right to subscribe for at least one-half

^a Assembly Report, New York, No. 136, February 7, 1834.

^b Report, p. 62.

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the stock;^a in three charters, 1828–1830, stock was to be subscribed by citizens of New Jersey exclusively; in 1832, citizens of Pennsylvania were given the privilege of subscription;^b in 1848, all outsiders were again excluded, and in a charter of 1855 it was provided that a majority of stockholders must always be residents of the State.^c

In Pennsylvania the charter of the Bank of Pennsylvania, 1793, required for the purpose of distributing ownership that books should be opened in Philadelphia for 2,000 shares, in Lancaster for 300, and in Reading for 200, and that no subscriptions should be received in Philadelphia for the two latter places until after ten days had elapsed. The omnibus act of March 21, 1814, which at one stroke created 41 new banks in different parts of the State, is evidence of the fear of concentrated banking power. There was a widespread jealousy and fear of foreign ownership. This was seen in the debate over the renewal of the charter of the First United State Bank; and Pennsylvania, in 1825, in rechartering the Bank of North America, prohibited any foreigner, save a citizen of Holland, to hold stock unless he had declared his intention of becoming a citizen. The general law of 1824 also debarred foreigners by prohibiting the transfer of stock to non-citizens of the United States, but as this was easily evaded the law was repealed in 1836. Again, the act of 1824, which divided the State into 27 banking districts, provided that on the first day of subscription only 2 shares could be taken by one person; on the second day not more

^a Acts, New Jersey, 49 Ass., p. 100, sec. 2.

^b Acts, New Jersey, 56 Ass., p. 58.

^c Acts, New Jersey, 79 Leg., p. 657, sec. 2.

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than 4, on the third day not more than 6, on the fourth day not more than 8, on the fifth day not more than 10, and on the sixth day and those subsequent, additional shares, provided the grand total was not more than 100. The charter of the Girard Bank, 1832, provided that no one should take more than 5 shares the first day, 10 shares the second, and 50 shares the third day; but notwithstanding these provisions there was great scandal in the awarding of stock; the privilege of acting as commissioner for the distribution of shares was valued at from \$500 to \$700, and the allotment occasioned a riot.^a

In Maryland, in chartering the Bank of Baltimore, 1795, the legislature demanded that books be opened in each of the counties, and limited the subscriptions by any one person to 20 in a single day.^b This became the usual practice in the organization of the early banks in that State; a committee was appointed to receive subscriptions at each county seat; persons non-resident in the county could not subscribe until after the lapse of a stated time; shares then remaining could be subscribed for by anyone, and if still untaken were advertised in the Baltimore papers.^c

Virginia restricted subscription in the Bank of Alexandria, 1792,^d to 50 shares, and not more than 25 in any one month. This State also, in 1812, required that all shares subscribed for must be held solely for the beneficial interest of the subscribers, any contract notwithstanding.^e

^a Niles, 42: 257.

^b Bryan, *History of State Banking in Maryland*, p. 26.

^c *Ibid.*, p. 30.

^d *Laws of Virginia*, 1792, ch. 76, sec. 18.

^e *Farmers' Bank of Virginia*, acts of 1812, pt. 1, ch. 7.

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Subscriptions were also apportioned among the leading cities of the State. In the general law of 1837, it enacted that if any bank outside the State purchased stock in a Virginia bank, such stock should be forfeited to Virginia for the benefit of internal improvements.^a Apparently this restrictive policy was successful, for in 1837, out of 1,892 stockholders in all the banks, only about 100 were non-residents.

In Ohio, by the charter of the Bank of Chillicothe, 1808, no one could hold over 40 shares or subscribe for more than 5 shares in one day.^b Efforts, however, to secure ownership to residents only were unavailing. In 1833 the capital of local banks held by non-residents was \$1,650,000, as against \$1,380,000 held by residents.

In the establishment of the State Bank of Indiana, 1817, subscriptions were opened in each county,^c and in 1834 it was provided that if there was an oversubscription deduction should be made from subscriptions over \$500 until all were reduced to that amount. By the general law of 1855 the majority of the stock of any bank must be owned by resident citizens of the State.^d

In Illinois the charter of the Bank of Illinois at Shawneetown, 1816, the first bank in that State, provided that no one person could take more than 10 shares on each of the first ten days of subscription; in a charter of 1818, however, shares could be purchased without limit. In the charter of the State Bank of Illinois, 1819, purchasers

^a Laws Virginia, 1836-37, ch. 82, sec. 81.

^b Laws of Ohio, 7:68.

^c Laws Indiana, 1817, ch. 41, sec. 3.

^d Laws Indiana, 1855, ch. 7, sec. 29.

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were limited to 500 shares at \$100 each. The bank commissioners in 1839 called attention to non-resident ownership of the State Bank of Illinois; in a total capital of \$3,645,000 the State held \$2,100,000, but of the remainder in private hands, outsiders controlled all but \$63,000. Missouri, in the charter of the Bank of St. Louis, 1813, provided that three-fourths of the capital should always be held by citizens either of Missouri or Illinois. In the charter of the Bank of Missouri, 1817, no restriction of this character, however, was imposed.

Kentucky bank returns carefully distinguished between home and non-resident ownership. For example, in 1838 the State owned 10,000 shares in the Northern Bank of Kentucky; residents, 6,419, and individuals registered at the Philadelphia and New York agencies, 13,581 shares.^a Foreign capital, also, was largely invested in Tennessee banks. In 1837 the State owned 5,984 shares in the Union Bank; residents, 3,236; and non-residents, principally in the East, 16,764 shares. In the Bank of Nashville there were 2,917 shares owned in the State, 10,050 on the books of the New York agency, 7,043 at the Philadelphia agency, of which 2,038 were held in England.^b

Alabama, in chartering two banks in 1818, required that not more than 5 shares be taken at a time, during the first six days of sale, and that no one be allowed to own more than 20 shares.^c In 1820, in the act of incorporation of the Bank of the State of Alabama, the capital was carefully apportioned among 10 towns. The stock of

^a Report of Bank Commissioners, Kentucky, 1838.

^b Report of Legislative Committee, Tennessee, 1837.

^c Territorial Acts, Alabama, 2d session, November 21, 1818.

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the Planters' Bank in Mississippi, 1830, apportioned the capital to different parts of the State, and provided that no one could subscribe for more than 30 shares on any one day during the first twenty-five days. Later, however, it appeared that these provisions were not enforced, and that the bank, instead of distributing its capital among the senatorial districts, had sought to engross the whole of it for the benefit of the management.^a By its original charter, foreigners were excluded from ownership, but in 1831 this restriction was removed. In Florida the charter of the Bank of Florida, 1828, also reserved certain blocks of stock for towns in which offices of discount were to be established, but it was easy to evade requirements as to citizenship within the State. Although Florida had such a restriction, a Walter Gregory, of Boston, became a nominal resident of Pensacola and subscribed for 1,705 shares of the 2,000 shares of the bank of that city. Eleven other residents took 45 shares and 250 shares were reserved for the Territory. Gregory actually owned only 621 shares, and the remainder of his subscription was owned in Boston, New York, and Philadelphia. As a matter of fact, a very large part of the capital of Florida banks was owned in the North. In 1851 the charter of the State Bank of Florida forbade any one to take more than 100 shares, until books of subscription had been open sixty days.

States, however, like Louisiana, which founded banks on loans through the sale of bonds, openly sought for outside capital. It was regarded as a profitable investment

^a Message of the Governor of Mississippi, 1838.

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to borrow at 5 or 6 per cent in order to earn dividends of from 7 to 10 per cent. In Louisiana in 1837, of the actual bank capital paid in there was due to Europe on State bonds \$13,854,000, and of bank stock there was held \$4,828,000. There was held in the United States outside of Louisiana \$7,965,000, and in Louisiana \$10,123,000.^a

III. STATE OWNERSHIP OF STOCK.

In nearly all States, even when they did not engage directly in banking on their own financial responsibility, provision was made in the charters requiring or permitting the State to subscribe for a portion of the stock of banks when organized. There were several reasons for this: First, the desire that the Government should share in the large profits which it was expected a bank would earn; second, that the State through ownership might have some voice in the management of banks, and thus possibly check policies which would be antagonistic to public interest; third, because ownership would place the State in the light of a favored customer when it desired to borrow; and fourth, because of the lack of private capital, which led organizers of banks to welcome financial support and cooperation on the part of the State.

The United States Government subscribed for \$2,000,000 or one-fifth of the capital of the first United States Bank. It was not, however, given the right to appoint any of the directors. The Federal Government likewise subscribed for one-fifth of the \$35,000,000 of capital of the second

^a See also Niles, 48:145.

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bank in 1816, and in this instance the charter provided for the appointment of five directors by the President.

The subject of state ownership in banks has been made the topic of a special investigation by Prof. G. S. Callender, and from his study the following paragraphs are summarized or quoted at length:

All of the older States, with the exception of New Jersey and two or three of the smaller New England States, owned more or less bank stock by 1812; Massachusetts had \$1,000,000; Pennsylvania, \$2,108,000; Maryland, \$540,000; and New York, Connecticut, and Delaware a small amount each. The Northern States ceased to make further investments of this kind at that time, though some of them continued to own their stock until a much later date. Pennsylvania did not dispose of hers until 1843; and the Southern, Southwestern, and Western States, which established governmental banks, held a much larger amount for a much longer time. "The Southern States, however, continued to accumulate holdings in bank stock until the civil war; Georgia had between three and four million dollars in 1839; South Carolina owned all the stock of the Bank of the State of South Carolina, which amounted to \$1,156,318; and a large part of Virginia's internal improvement fund, which amounted to \$1,185,000, was made up of bank stock. The same policy was taken up in the Western States about 1820. In these States, however, the funds invested in bank stock were not, as in the East, derived from revenue; but the States sold their bonds to secure the necessary funds. The first State to do this on a considerable scale

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was Louisiana in 1824; and between that date and 1840 the Western and Southwestern States, including the Territory of Florida, issued over \$65,000,000 of bonds to provide banking capital to corporations. Thirteen of the States invested more or less of their shares of the surplus revenue of 1837 in banking. Ten of these were Southern States. * * * The motive which caused this wide-spread connection of the States with the banks was not, however, the same in all sections of the country. In the older States, both North and South, it was not primarily, if at all, due to the desire to encourage the growth of banking. Banks needed no such encouragement in those States. On the contrary, they were regarded as very profitable enterprises and the investment of capital in them as a distinct privilege. * * * In the newer States, where capital was more scarce, other motives played a considerable part. The people were anxious to furnish a circulating medium, and also to provide banking accommodations to the commercial classes, as well as loans to farmers. But in all, except the cotton States of the Gulf region, the desire to secure for the benefit of the public the large profits to be earned in the banking business was an important, if not the most important, motive which led the States to invest in these industries. Thus, when Indiana and Illinois began their system of internal improvements, they both increased the capital of certain banks and authorized the States to subscribe for the new capital. * * * These States could borrow money at 5 or 6 per cent interest, and the banks earned from 7 to 9 per cent dividends. They found it profitable,

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therefore, to provide for the payment of a part of the interest on their internal improvement debts by selling bonds and investing the proceeds in bank stock. A similar motive influenced the action of Kentucky and Tennessee. * * * In the Southwest the situation was different. The demand for capital here and the difficulty of obtaining it were, perhaps, greater than in any other part of the country. * * * The planters of this region had to attract capital from the North and from Europe; and for this purpose the credit of individual planters or of such corporations as could be formed in a new country was as inadequate as it was in Northern States to secure funds for canals and railways. Nothing was left but to make use of public credit to supply this deficiency, and every new slave State in the South from Florida to Arkansas established one or more banks and supplied all or nearly all of their capital by a sale of state bonds. Many of the banks were known as 'property banks,' and were designed especially to furnish loans to planters."^a

In addition to this instructive summary by Professor Callender, the following details of State practice may be given. Beginning with the charter of the Union Bank of Boston in 1793, Massachusetts retained the right to State stock in most of the banks established, up to one-third of their capital. In 1812 the State owned \$1,000,000 out of a total of \$8,000,000 of bank stock, and this right of State ownership was continued for many years. As a rule, the

^a G. S. Callender: *The Early Transportation and Banking Enterprises of the States in Relation to the Growth of Corporations*. *Quart. Jour. Econ.*, 17:111-162.

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charter gave the State the additional privilege of subscribing for not more than 50 per cent of the capital besides that named in the act of incorporation. This was confirmed in the general law of 1829. The State was also given representation on the Board of Directors in proportion to the capital. The State of Rhode Island never subscribed for bank stock, but like some other New England States, bought such stock for school funds. In Connecticut, the charter of the Hartford Bank, 1792, gave the State the right to subscribe for 40 out of the 250 shares, with power to appoint two directors.^a

The same option was reserved in New York charters; as, for example, in that of the Mechanics' Bank in New York City, 1810, where the State had the privilege of subscribing for one-sixth of the capital. Down to 1833 the State owned \$85,000 of stock in institutions which had become insolvent.^b By the charter of the Trenton Banking Company of New Jersey, 1810, the State was authorized to subscribe for \$20,000,^c and in 1812 one-half the capital in five banks was reserved for the State.^d

Pennsylvania followed a consistent policy of subscribing to the capital of local banks. In 1793 it subscribed for one-third of the capital of the Bank of Pennsylvania^e and within a few years it obtained as dividends on shares which it held nearly enough to pay all its expenses.^f

^a Woodward: *The Hartford Bank*, p. 19; for similar action in 1803, see pp. 82-84.

^b Assembly Report, New York, No. 283, April, 1833.

^c Laws of New Jersey., 35 Ass., 1 sess., 249.

^d Laws of New Jersey, 36 Ass., 2 sess., p. 5, sec. 3.

^e Smith, *Laws of Pennsylvania*, 3:97.

^f Sumner, *History of Banking*, 1:44.

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The Philadelphia Bank, 1803, permitted the State to subscribe for \$300,000 of stock out of a total of \$2,000,000 and gave it the privilege of subscribing \$200,000 more at the end of four years and a similar amount at the end of eight years. The State could appoint 6 of the 22 directors. An act of March 10, 1810, provided that when the funds in the State Treasury rose above \$30,000, the surplus should be invested in the stock of the Bank of Pennsylvania, and in that year the State owned \$1,600,000 of bank stock. In 1813 the State received \$200,000 in dividends, equivalent to two-fifths of the entire revenue.

State ownership of stock, while it frequently brought a welcome addition of capital, had its disadvantages; particularly was this so when the State was given a voice in the appointment of a certain number of directors. In 1829, when complaint was made that the Bank of Pennsylvania did not loan as much as was desired to the State, it was admitted that State directors introduced a division of interest; there was a "pertinacious, persevering, and indiscriminating opposition to almost any prominent measure which is proposed by directors elected by stockholders."^a

In Maryland, with the exception of the Bank of Maryland, the State reserved the right to subscribe a specified amount in each bank, and it took advantage of this in the case of the Bank of Baltimore in 1803. By 1811 it owned stock in each of the Baltimore banks and in three country banks, but after that year it ceased to make subscriptions.^b

^a Address to Stockholders of the Bank of Pennsylvania, December 22, 1829, p. 17.

^b Bryan: History of State Banking in Maryland, p. 30.

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This policy was adopted to give the banks a public character. In the Mechanics' Bank, for example, 1806, it was provided that when the State had subscribed \$40,000 of the total capital of \$1,000,000, she should be entitled to two directors, and when \$100,000, to three directors. The directors were to be elected by the General Assembly by ballot. In Virginia, the charter of the Bank of Virginia, 1804, provided that the State should subscribe \$300,000, or one-fifth of the capital issued, borrowing that amount from the bank at 4 per cent. In 1837 the State was authorized to subscribe for one-half the capital of several new banks then organized.^a

In the charters of North Carolina, the State, as a rule, was allowed to own a certain percentage of stock. In the Bank of the State, the Government took one-third; in the Bank of North Carolina, it took \$2,000,000 of the \$3,500,000 capital, and the charter provided that the State should have a vote proportional to its stock, whereas individual stockholders voted in a decreasing scale. Alabama, which began her banking legislation as a territory, in 1816 authorized the Government, in the first three charters, to subscribe for one-tenth, two-fifths, and one-fifth of the stock, respectively. The State, however, did not take advantage of this; but the constitution of 1819 required that two-fifths of the capital of every bank should be reserved to the State. In the Planters' Bank of Mississippi, 1830, the State took two-thirds of the capital, paying in bonds which the bank was authorized to sell. It was provided that the Government should appoint seven directors and

^a Laws of Virginia, 1836-37, ch. 83.

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the stockholders six. The Commercial Bank of New Orleans, 1813, which was organized to construct water-works, as well as to do a banking business, reserved one-sixth of its capital to the State.

In Ohio, the charter of the Bank of Marietta, 1808, reserved the right to the State to subscribe for one-fifth of the capital. In Kentucky, the State subscription to the capital of the Bank of Kentucky, 1806, was placed at one-half. In Indiana, the charter of the State Bank of Indiana, 1817, gave the State the right to subscribe for \$375,000 out of a total capital of \$1,000,000.^a

IV. SUBSCRIPTIONS BY RELIGIOUS AND EDUCATIONAL SOCIETIES.

In a few States, banks were utilized to aid the cause of religion and education. For example, in Connecticut in 1806, it was enacted that subscriptions for an increase in the capital of the Hartford Bank be received at par from the funds of schools and ecclesiastical societies or other incorporations for charitable purposes. The shares thus taken were not transferable, but the institutions could surrender their certificates at any time at par. This arrangement, originally devised to attract capital when the bank was seeking to extend its operations, proved to be an embarrassment to the bank. The societies were protected in case the stock fell below par, and until the maximum limit of authorized capital was reached could obtain stock on much more favorable terms than private individuals who had to make their purchases at a pre-

^a Laws, Indiana, 1817, ch. 41, sec. 2.

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mium.^a Efforts to repeal this privilege were unsuccessful and the plan continued until the establishment of a national banking system. New York imitated this plan, and by an act passed in 1813 allowed certain colleges to subscribe for stock in a number of banks at par. The charter of the Bank of Florida, 1829, provided that \$100,000 of the maximum capital of \$600,000 should be reserved to be taken by the governor for the benefit of a seminary of learning.^b The act of incorporation of the Merchants' and Planters' Bank of Augusta, Ga., 1827, gave any religious, charitable, or literary institution, incorporated by the State, the right to deposit not more than \$50,00 and receive State scrip for it at par, and entitled it to dividends.^c

V. LENGTH OF CHARTER.

With few exceptions, the grant of a banking privilege under a corporate charter was limited as to time. Corporations were a new form of business organization, and legislatures were disposed to view them with caution, if not with jealousy and suspicion.

The charter of the Massachusetts Bank, granted in 1784, the first in that State, was perpetual, but later, in 1812, with the consent of the bank, it was limited to a definite term of years. Subsequent charters ran for ten years, and were then extended, so that all would expire

^a Woodward, *The Hartford Bank*, pp. 86-88; Sumner, *History of Banking*, 1: 42.

^b For similar subscriptions to stock of Bank of Kentucky, see Duke, *History of the Bank of Kentucky*, 16.

^c Sumner, *History of Banking*, 1: 179.

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in 1812. 1831 was next set as the date of termination of grants, and then 1851 was established as the beginning of a new period. Twenty years, indeed, became a favorite term, no doubt due to the fact that this was the period provided for in the charters of both the First and Second United States Banks. In Rhode Island^a all charters were unlimited, and, as a rule, no time limit was set in Connecticut, but in that State the legislature could amend or repeal at any time. The New Hampshire Bank obtained a charter for fifty years.

New York, in 1791, adopted the twenty-year period for the Bank of New York. New Jersey, in 1804,^b followed the example set by New York in regard to time, and continued it in subsequent charters.^c In Pennsylvania, the Bank of North America, 1787, received a grant for fourteen years; the Bank of Pennsylvania, 1793, for twenty years; the Philadelphia Bank, 1804, for ten years, later extended to twenty; and the 41 new banks created in 1814, for eleven years. In issuing the charter of the Bank of North America in the same year, the legislature reserved the right to amend the charter at any time, on condition of refunding a proportionate part of the bonus which the bank was called upon to pay.^d

The Bank of Maryland, 1790, secured a perpetual charter; in 1795, however, when the Bank of Baltimore was established, its term was restricted to twenty years.

^a Stokes, *Chartered Banking in Rhode Island*, p. 10.

^b Newark Banking and Insurance Company; same period adopted in the banking law of Jan. 28, 1812; *Laws of New Jersey*, 36 Ass., 2 sess., pt. 4, sec. 2.

^c Acts, N. J., 53 Ass., p. 65; Acts, 74 Ass., Legis., 147, sec. 16.

^d Lewis, *The Bank of North America*, p. 89.

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Virginia, in its earliest experience with banks, fixed ten years as a limit,^a but in 1814, the legislature gave to the Bank of Virginia a charter for fifteen years; and in 1817, fixed upon seventeen years for two other institutions. In 1851, twenty years became the established rule.^b In 1845, banks in Florida were limited to twenty years, with no renewal or extension. Louisiana, in 1811, selected fifteen years; Kentucky, in 1806, made the same limit.^c Ohio, in the charter of the first bank incorporated, limited the period to ten.

In Indiana, the State Bank of Indiana, in 1817, was given eighteen years, and on its extension in 1834, twenty-five years. The general law of 1855 provided that the certificate of incorporation should specify the period of existence.^d In 1855, twenty years was adopted for the Bank of the State of Indiana.

VI. SCOPE OF BUSINESS.

As a rule, the scope of business which a bank could carry on was during the earlier period defined in but general terms. It was the custom to justify the organization of a bank by the facilities which it could render to the public and to mercantile interests. For example, the preamble of the act of incorporation of the First United States Bank, 1791, justifies the organization of the bank on the ground that it will be conducive to the successful conducting of the national finances; will give facility to

^a Bank of Alexandria, 1792; Bank of Richmond, 1792; Bank of Alexandria, 1801, extension.

^b Laws, Va., 1850-51, ch. 58, sec. 11; ch. 59, 61, 62.

^c Bank of Kentucky at Frankfort.

^d Laws, Ind., 1855, ch. 7, sec. 18.

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the obtaining of loans by the Government in sudden emergencies, and will be productive of considerable advantage to trade and industry in general. The reason for the granting of a charter to the Mechanics' Bank of Baltimore in 1806 was stated in the charter to be for the promotion of the mechanical and manufacturing interests of the State. Many charters designated the scope of operations which banks could engage in by intrusting to them "usual banking powers." As banking powers were not clearly defined, there was opportunity for banks to enlarge their business in almost any direction desired. Only gradually, as banks sought to enlarge their financial operations, did charters specify with precision the acts which they could perform. In 1839 a specific definition of the powers of banks of New York was to be found in the charters of only 66 out of 97 banks. The other 31 charters were granted previously to 1825 and either conferred bank powers in general terms or limited the operations of these institutions to the ordinary business of banking. This change is evidence of the growing caution of the legislature. It was customary to restrict operations to dealings in notes, bills of exchange, and bullion. Transactions in goods or commodities were generally excluded unless they were received for loans which were not redeemed at maturity.^a

The holding of real estate, except what was necessary for the conduct of business or obtained in satisfaction of debts, was generally prohibited. The Portland Bank of Maine, 1809, was permitted to hold any amount of land in

^a Sen. Doc. New York, No. 87, April 11, 1839.

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payment of debts, provided that not more than one-third of the capital thus invested was in "fee simple."^a The Commonwealth Bank of Boston, 1824, could invest \$50,000, or one-tenth of its capital, in lands and real estate, and by the general banking law of Massachusetts in 1829, banks could hold real estate not exceeding 12 per cent of the capital. In Pennsylvania the amount which could be expended for a banking house was also expressly limited.^b

There was less agreement in regard to dealings in public stocks. Some feared that banks might speculate in such securities, lower the price of government stock when loans were sought, and raise the price when purchases were required for sinking funds. The charter of the First United States Bank permitted the sale, but not the purchase, of government stock. The articles of association of the Bank of New York, 1784, forbade the bank to negotiate any foreign bill of exchange or to advance a loan to any foreign power.^c The charter of 1791 omitted the restriction in regard to foreign bills, but forbade the bank from dealing in the stock of any State or of the United States.^d By special act in 1797 the bank, however, was authorized to purchase certain United States stock held by the State.^e The Hartford Bank, in its early charter of 1792, was permitted to invest in United States stock without limitation.^f By act of Congress,

^a Stackpole, *Sound Currency*, 7:58.

^b See act of March 25, 1824, where the sum for a Philadelphia bank was set at \$50,000 and for one outside at \$30,000.

^c Domett, *Bank of New York*, p. 13.

^d *Ibid.*, p. 54.

^e *Ibid.*, pp. 132-133.

^f Woodward, *The Hartford Bank*, p. 19.

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1817, banks in the District of Columbia could not deal in stocks of the Federal Government or of the several States. As late as 1862 the bank commissioners of Massachusetts thought that it was clearly against the law and public policy for banks to buy and sell without restriction public securities of remoter States or of municipal and corporate bodies, as this led them into dangerous paths of speculation.

As indicated above, there was quite a difference in the variety of powers granted to various banks in New York. Not until 1825 did a charter contain the restrictive clause: "But the said company shall have and possess no other powers whatever, except such as are expressly granted by this act." And at this date the Commercial Bank of Albany was prohibited from receiving the transfer or pledge, not only of its own stock, but of the stock of any other incorporated company. In 1839 a legislative committee made an analysis of the several charters with the following results: Ninety-two banks out of 97 were prohibited from purchasing, holding, or conveying any real estate, except such as was required for the convenient transaction of business, or such as was mortgaged to them by way of security for loans previously contracted, or conveyed to them in satisfaction of debts, etc.; 4 of the other 5 banks were originally incorporated for other than banking purposes; 88 of the 97 banks were prohibited from dealing or trading directly or indirectly, in buying or selling any merchandise, or in buying or selling any United States or state stock except in selling the same when pledged by way of security. Of the remain-

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ing 8, 3 were prohibited from dealing in United States and New York stocks, 2 from dealing in United States stock, 3 were authorized to hold stocks, and 1 was unrestricted. The three institutions authorized to hold stocks were incorporated for other purposes than banking. In four instances, during the ten years beginning with 1812, the prohibition to deal in stocks was superseded for special purposes, so as to permit subscription for national and state loans and for aid in behalf of canals. For eighteen years, however, the authority to subscribe for state stocks was not renewed, except in 1837 to permit the banks to subscribe for certain canal loans, the object of which was to save the banks from suspension of specie payments.^a

The charter of the Bank of Pennsylvania, 1793, forbade the purchase of any public stock, save in 1802, when an exception was made in favor of United States securities. In the charter of the Farmers and Mechanics' Bank of Philadelphia, 1809, exception was also made in favor of the stock of companies incorporated in the State for the improvement of roads or internal navigation. The act of 1814 gave to the new banks the right to hold stock of other banks, but this, together with the holdings of other public securities, could not exceed 20 per cent of the total stock. This provision was repeated in the banking act of March 25, 1824.^b

Virginia, in 1812, permitted the Farmers' Bank of Virginia to purchase its own stock up to 1,500 shares, on condition that it sell the same as soon as possible at par.

^a Sen. Doc., New York, No. 87, April 11, 1839.

^b Article xiv.

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In a charter of 1817 a bank was forbidden to purchase any negotiable securities except its own stock;^a but in 1837 a general act prohibited the purchase of a bank's own stock under penalty of forfeiture. Florida, in 1828, forbade the Bank of Florida to purchase any public stock except its own, which was to be sold again as soon as convenient. For engaging in the sale of merchandise there was a penalty of treble the value of the goods.

Some of the southern banks which were organized expressly to aid the agricultural interests were naturally given powers as to investment and loans which were denied to commercial banks. The Union Bank of Louisiana, 1812, was the model of several institutions which were established to make loans to owners of slaves and real estate. The Planters' Bank in Mississippi, 1830, like most of the banks in that State could hold lands, rents, tenements, goods, chattels, effects, etc., up to \$6,000,000, or double the capital. Though not intended, this grant was later, in the speculations of 1837, construed to justify extensive operations in cotton, including even the purchase of the staple.^b Georgia found it necessary in 1840 to forbid explicitly banks from dealing in cotton or other commodity as security for loans. In 1855 the general banking law of Indiana forbade loans on real estate.^c

Frequently banks were organized to further the fortunes of an internal-improvement company, and were authorized to invest in some particular stock. For example, Rhode Island in 1831 chartered the Blackstone

^a Laws of Virginia, ch. 39, sec. 11.

^b Message of the Governor of Mississippi, 1839.

^c Laws, Ind., 1855, ch. 7, sec. 20.

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Canal Bank and empowered it to invest \$150,000 in the stock of the canal company.^a In 1832 the Quinebaug Bank of Connecticut was required to subscribe \$100,000, or one-fifth of its capital, to the stock of the Boston, Norwich and New London Railroad Company. The Commercial Bank of New Jersey, 1822, was authorized to set apart a portion of its capital for carrying on seal fisheries.^b The extension of charters in Maryland in 1813, was conditioned on investments in the stock of a turn-pike company, and later this method of securing financial support was frequently resorted to.^c Virginia, in 1833, authorized two of her banks to subscribe for stock in an internal-improvement company.^d

During the first part of the last century banking privileges were frequently granted to transportation companies. This has been described by Cleveland and Powell,^e from whose study the following condensed account is taken:

"As early as 1814 Maryland chartered the Susquehanna Bank and Bridge Company, with power to employ half its funds in the banking business. In an amendment to the charter of the Delaware and Hudson Canal granted by New York in 1824 the company was given the right to exercise banking powers during a period of twenty years. New Jersey the same year granted a charter to the 'Morris Canal and Banking Company' which gave

^a Stokes, *Chartered Banking in Rhode Island*, p. 37.

^b Repealed in 1825.

^c Bryan, *History of State Banking in Maryland*, pp. 45-47.

^d *Laws, Va.*, 1832-33, ch. 89; see also laws 1850-51, ch. 89, sec. 4.

^e *Railroad Promotion and Capitalization*, pp. 167-173.

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the enjoyment of banking functions through a term of thirty-one years. Maine chartered the 'Canal Bank' in 1825, with authority to invest one-fourth of its paid subscriptions in the stock of the canal company. Connecticut in 1832 chartered the Quinebaug Bank as an adjunct to the Boston, Norwich and New London Railroad.

"At a single session of the territorial legislature in 1835 Michigan conferred banking powers upon four railroad companies. Stockholders of the River Raisin and Grand River Railroad were constituted a corporation under the title 'Bank of Tecumseh,' with a capital stock of \$100,000, or two-thirds that of the railroad. This bank was to be managed by the directors of the railroad, who were to convey to it the whole of the railroad stock, and to give security for the redemption of notes and debts before banking operations could be commenced. The Ohio Railroad charter of 1835 contained a provision 'that the funds of said company shall be paid out in orders drawn on the treasurer, in such manner as shall be pointed out by the by-laws of the company; and that all such orders for the payment of money so drawn shall, when presented to the treasurer, be by him paid and redeemed.' Without collecting a dollar from the stockholders, and with an empty treasury, the company, under authority of this clause, began banking operations, and successfully maintained a large circulation. Laborers and contractors were paid in notes, and from the proceeds of the bonds of the State received as a subsidy some of these notes were redeemed. When the company suspended there had been no work of permanent character done on the road, and

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there were outstanding several hundred thousand dollars in worthless currency.

“The first railroad corporation authorized in Texas was the ‘Texas Railroad, Navigation and Banking Company,’ which was chartered by the first congress of the republic to connect by railroad and canal the waters of the Sabine and the Rio Grande, but the charter was forfeited. Both Louisiana and Mississippi were liberal in their grants of the banking power, not only to railroads, but to industrial corporations as well. Louisiana in 1834 conferred banking powers upon the Clinton and Port Hudson Railroad, and provided for a note issue which might reach double the amount of its banking capital. The following year this State authorized the New Orleans and Carrollton Railroad to establish ‘five offices of discount and deposit’ in different towns, and chartered a new corporation, the ‘Atchafalaya Railroad and Banking Company,’ with power to open a bank in the parish of West Feliciana. In 1836 the Pontchartrain Railroad received a grant of the banking power. In Mississippi we have this picture of the results of using banks as agencies of railroad financing: ‘From December 20, 1831, when banking privileges were conferred on the West Feliciana and Woodville Railroad, until the crash came in 1837, Mississippi was gridironed with imaginary railroads and beridden with railroad banks. In these enterprises there was more watered stock sold than there were cross-ties laid; reckless speculation brooked nothing as prosaic as the actual construction of railroads, on the successful

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operations of which it was supposed fabulous dividends would be declared.'

"When the lines from Savannah to Macon and from Augusta to Athens were first projected, capital requirements were so great that appeals for state aid were made by both the Central and the Georgia railroads. Failing to receive the desired aid, they applied for banking privileges, which were granted. The names were therefore changed to the 'Central Railroad and Banking Company,' and the 'Georgia Railroad and Banking Company.' One-half of the capital of these companies could now be devoted to banking, and notes could be issued to three times the banking capital.

"As an adjunct to the Louisville, Cincinnati and Charleston Railroad by which it was planned to connect Charleston with the Ohio, the 'South Western Railroad Bank' was chartered in South Carolina, North Carolina, and Tennessee in 1836 and 1837. Kentucky granted a charter to the railroad, but in express terms prohibited banking, and the bill to incorporate the South Western Railroad Bank in that State failed by six votes. This bank was capitalized at \$6,000,000. A unique feature of the enterprise was the issue of the shares in the bank inseparably connected with the shares of the railroad, so that everyone who held \$100 of stock in the railroad was required to subscribe \$50 toward the capital of the bank. Forfeiture of either share therefore worked forfeiture of both. The bank went into operation in 1839, and to its stock South Carolina subscribed \$500,000."

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VII. VOLUME OF NOTES.

The restrictions laid down by early charters in regard to the amount of notes which could be issued were exceedingly vague and lax, and little protection was given to the currency. Many of the acts of incorporation did not make specific requirements, but covered the point indirectly through limitations in the amount of indebtedness, including deposits. The charter of the First United States Bank provided that "the total amount of the debts which the said corporation shall at any time owe, whether by bond, bill, note, or other contract, shall not exceed the sum of \$10,000,000 (i. e., the capital) over and above the moneys actually deposited in the bank for safe-keeping." In the charter of the Bank of England, which served in many respects as a model for the First Bank, indebtedness could not exceed the capital, irrespective of deposits. In the English joint-stock banks there was no limitation during the earlier part of the nineteenth century.^a

The States were generous in their grants of indebtedness. At the outset this limitation was generally set at two or three times the capital. This amounted to practically no limitation at all, at least upon banks with a large capital, and admitted an issue of notes out of all proportion to the specie fund. Naturally, it afforded an opportunity for a wide range and violent fluctuations in the amount of outstanding currency, depending upon applications for discount. Twice the capital actually paid in, exclusive of deposits, was the rule followed by

^a Gilbart, *History of Banking in America*, p. 73.

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Massachusetts banks down to 1811, when for many institutions the note issue was reduced to 50 per cent in excess of the capital, exclusive of deposits.^a Between 1825 and 1828 nearly 30 banks were limited to 100 per cent, and in the latter year the general rule was made 125 per cent. This continued until 1858, when circulation was restricted to the amount of capital. Connecticut, in the charter of the Hartford Bank, 1792, adopted a more conservative ratio of 50 per cent of the capital and deposits combined, and this proportion was continued in subsequent charters.^b Circulation based on deposits obviously opened the way for abuses. In 1837 the bank commissioners reported that the Stamford Bank had created fictitious deposits in order to increase its note issues, and later, in 1853, they recommended that this rule of measuring circulation be abandoned; only three banks in the State at that time resorted to this method, but the opportunity should be denied. One bank was cited where the circulation had been carried to \$300,000; recourse was had to sight checks drawn on individuals in New York by the president of the bank and deposited in the hands of the cashier, payable to his order; none of these, however, had ever been out of the bank or presented for acceptance; deposit was indebtedness and circulation was indebtedness; to maintain a circulation on deposits was to build up one species of indebtedness on the basis of another. In 1855 circulation was restricted to 125 per cent of the capital and in 1858 to 75 per cent.

^a For statistics see Root in *Sound Currency*, 2:4.

^b Woodward, *The Hartford Bank*, p. 19.

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In Rhode Island the charter of the Providence Bank, 1791, placed no limitation of any sort upon circulation, and in harmony with the principles of freedom which governed legislation in that State for many years, several subsequent charters were silent on this point. In 1805 indebtedness was limited to capital plus the deposits.^a In 1820 issues were limited to the paid-in capital, and in 1837 a more elaborate set of percentages on capital was adopted as follows:

Banks with a capital of—	Per cent.
\$50,000.....	75
\$50,000 to \$120,000.....	65
\$120,000 to \$200,000.....	40
\$200,000 to \$300,000.....	30
\$300,000 to \$400,000.....	25
\$400,000 to \$500,000.....	20

In 1859 the limit was made 65 per cent for all banks.

In New Hampshire circulation was based on capital, and in 1825 in the charter of the Commercial Bank of Portsmouth the issue could not exceed the capital under penalty of \$10,000. In 1838 a law was passed providing that loans made on a pledge of bank stock should be construed as a diminution of capital in determining the volume of notes. In Vermont, after 1840, circulation was limited to double the capital.

Maine, in 1831, made 150 per cent of the capital the rule of maximum issue, but in 1838 classified the banks according to capital and reduced circulation to ratios ranging from 66⅔ to 100 per cent. In 1846 the circulation in excess of 50 per cent of the capital was limited to three times the specie held, and the total circulation to capital

^a Stokes, *Chartered Banking in Rhode Island*, p. 21.

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plus the specie. As a penalty for overissue, a bank forfeited 10 per cent.

In New York the Bank of New York, 1791, was given a more generous privilege and indebtedness ran to three times the capital, exclusive of deposits. In 1829, under the safety fund act, this proportion was reduced to twice the capital. In 1834 a legislative committee suggested the advisability of still further restricting the issues to not exceeding capital; and in that year several charters were granted in which the limitation was fixed at one and a half times the capital. Under the law authorizing suspension of specie payments in 1837, circulation was restricted so that the volume of notes possible under previous laws was reduced from \$69,000,000 to \$30,000,000. In the same year, by the new banking act, provision was made for note issues according to capital, as follows:

Capital.	Notes.
\$100,000	\$150,000
120,000	160,000
150,000	175,000
200,000	200,000
250,000	225,000
300,000	250,000
400,000	300,000
500,000	350,000
600,000	450,000
700,000	500,000
1,000,000	800,000
1,490,000	1,000,000
2,000,000	1,200,000

New Jersey as well as Pennsylvania, in the general banking act of 1824, established twice the capital as a ratio, and this proportion was to be found also in Mary-

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land.^a For one year, 1818-19, New Jersey tried a stricter rule by limiting note issues to double the specie and notes of banks on hand which commanded specie.^b Maryland, in 1837, enacted that after resumption circulation should be limited to paid-in capital.^c

Virginia, in the charter of the Bank of Alexandria, 1792, allowed four times the capital;^d in a charter of 1812 this was reduced to three, and in 1817 to double. This latter ratio continued in that State and was reenacted in a general law of March 22, 1837. The latter act also limited the volume of notes not to exceed five times the specie.^e

The prevailing ratio in the Southern States was three times.^f Georgia, however, in the charter of the Central Bank, 1828, proportioned the volume to the amount of specie, notes of other banks in the State, and notes of the United States Bank which were held in its possession. In a bank convention held in 1837 the banks agreed voluntarily to limit their circulation to paid-in capital and specie in hand. In 1840 an act was passed in Mississippi (February 21), providing that no bank should issue more than three times the specie in its vaults. In Louisiana the banks of New Orleans in a convention of 1838 resolved by agreement that the circulation of each bank should be based on the amount of capital paid in and the accumu-

^a Bryan, *History of State Banking in Maryland*, p. 32.

^b Priv. Acts, N. J., 42 Ass., 1 sess., p. 60; Priv. Acts, 43 Ass., 2 sess., p. 16.

^c Acts, Md., 1837, ch. 315.

^d Laws, 1792, ch. 76, sec. 13.

^e Laws, 1836-37, ch. 82, sec. 2.

^f Sumner, *History of Banking*, 1:45.

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lated profits. The rates assigned to each bank varied from 25 to 50 per cent of this amount.

Ohio did not make any restriction upon note issues until 1812, when three times was the ratio adopted.^a In 1839 circulation was limited to three times the specie. Michigan, in 1837, adopted a scale like that of Rhode Island, basing circulation upon capital according to the following ratios:

Capital.	Circulation.
\$20,000	\$30,000
50,000	75,000
65,000	80,000
100,000	130,000
150,000	175,000
200,000	200,000

and for banks with capital above this amount, circulation to be the same as capital. Kentucky in 1858 limited circulation to paid-in capital. Missouri, in the charter of the Bank of St. Louis, 1813, also limited indebtedness to twice the capital stock.

There was a marked variation in the exercise of the note issue function between banks in the country and those in cities. The latter had larger deposits and capital in order to make loans, and thus made less use of notes. This difference between banks in thinly settled districts and districts covered with towns and cities is seen in a comparison prepared by Stokes between the three northern and the three southern States of New England:^b

^aCharter of the Bank of Muskingum.

^bStokes, *Chartered Banking in Rhode Island*, p. 23.

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[Thousands omitted.]

	Year.	Capital.	Circulation.	Percentage.
Maine.....	1820	\$1,600	\$1,400	88
New Hampshire.....	1831	2,000	1,100	55
Vermont.....	1834	920	1,460	159
Average.....				88
Massachusetts.....	1820	10,600	2,600	25
Rhode Island.....	1821	3,200	675	21
Connecticut.....	1834	6,800	2,400	35
Average.....				32
Maine.....	1855	7,300	5,100	70
New Hampshire.....	1855	4,400	3,600	82
Vermont.....	1855	3,600	3,700	103
Average.....				80
Massachusetts.....	1855	58,600	23,100	39
Rhode Island.....	1855	18,700	5,400	29
Connecticut.....	1855	17,100	6,800	40
Average.....				37

In 1834, the banks in Maine, New Hampshire, Connecticut, and Massachusetts, outside of Boston, had a circulation of about one-half of their capital, while that of the Boston banks was about one-sixth. In the analysis of these figures it is to be noted that the restrictive laws relating to circulation, while different in point of time, were very similar; that the Suffolk system of redemption extended over the entire section, and that the methods of paying in capital through stock notes did not vary greatly.

The same difference between city and country banks in the exercise of note issues is to be observed in other

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sections. In New York, for example, in 1820, the Washington and Warren Company, a country bank which had a paid-in capital of \$176,000 and only \$201 in deposits had \$186,000 in notes. The Bank of Geneva, with \$100,000 capital and deposits of \$21,500, had \$187,600 in notes.^a In 1829, eleven city banks with a paid-in capital of \$11,252,000 had a circulation of \$3,529,000, while eleven country banks with a capital of \$2,906,000 put out \$3,138,000 in notes. In Wisconsin, to use a western illustration, fourteen country banks at a later date had note issues equal to 90 per cent of their capital, as compared with the Milwaukee banks, which had a little over 50 per cent of their capital in notes.

During the earlier years of the century, there was a common notion that the volume of currency should bear a certain proportion to the annual product of industry; as to the exact ratio, however, there were wide-spread differences of opinion, writers varying from one-fifth to one-thirtieth. In a report made by Mr. Benjamin Hazard, chairman of a legislative committee in Rhode Island, 1826, the average of these extremes, or one-eighteenth, was accepted as a possible criterion. It was then estimated that the annual product was probably not over 7 per cent of the gross national capital. As ratable property in Rhode Island amounted to \$32,640,000, 7 per cent of this would be \$2,284,000. This was about one-fifth of the authorized banking capital, and it was consequently concluded that the note circulation of that State, instead of one-eighteenth, amounted to nearly two-thirds of the

^a Report of Committee on Currency, Assembly Journal, 1820, pp. 468-469.

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annual product, a volume far in excess of what was desirable.

This same idea was accepted in a report of a select committee of the Maryland legislature, to which was referred, in 1830, memorials of a large number of citizens praying for the establishment of a state bank.^a It was argued that the welfare of the people depended on maintaining a proper equilibrium between the total amount of property and the medium by which that property was exchanged. Whenever the volume of money was suffered to fall below its due proportion to the whole property of the people so in the same degree was their industry checked, their enterprise abated, their public works embarrassed, and their prosperity withered.^b

The following table shows the actual circulation compared with circulation permitted in the New England States:

[Sound Currency, Vol. 8:215; No. 4, December, 1901.]

1840.

State.	Banks.	Capital.	Actual circulation.	Circulation permitted.
Massachusetts.....	115	\$33,750,000	\$9,112,882	\$42,187,000
Rhode Island.....	62	9,880,500	1,719,230	5,000,000
Connecticut.....	31	8,806,204	2,325,589	13,209,000
Maine.....	49	4,671,500	1,224,658	3,500,000
New Hampshire.....	27	2,837,508	1,088,750	2,837,000
Vermont.....	17	1,196,770	1,099,784	3,590,000
Total.....	301	61,142,482	16,570,893	70,323,000

^a Teackle's Report.

^b See also veto message of governor of Mississippi, Feb. 15, 1838.

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1850.

State.	Banks.	Capital.	Actual circulation.	Circulation permitted.
Massachusetts.....	126	\$36,925,050	\$17,005,826	\$46,156,000
Rhode Island.....	63	11,716,337	2,553,865	6,000,000
Connecticut.....	37	9,152,801	4,888,029	13,729,000
Maine.....	32	3,248,000	2,654,208	3,050,000
New Hampshire.....	22	2,203,950	1,751,096	2,203,000
Vermont.....	27	2,197,240	2,856,027	4,395,000
Total.....	307	65,443,378	31,709,051	75,533,000

1860.

Massachusetts.....	178	\$66,482,050	\$25,012,745	\$83,102,000
Rhode Island.....	91	20,865,569	3,588,295	13,562,000
Connecticut.....	74	21,606,997	7,702,436	16,205,000
Maine.....	68	7,506,890	4,149,718	5,765,000
New Hampshire.....	51	4,981,000	3,332,010	4,931,000
Vermont.....	44	3,872,642	3,784,673	7,745,000
Total.....	506	125,315,148	47,539,877	131,310,000

Notwithstanding the liberal provisions which charters granted for circulation, banks in the Northern States, either through policy or compulsion, rarely issued the legal maximum. Restriction by statute was operative upon the smaller banks, but was of little need in controlling the larger institutions which had the legal capacity to supply by far the greater part of the circulating medium. These latter were effectually restricted by the rapidity with which the notes were turned back for redemption. For example, in Rhode Island note circulation never exceeded one-third, and on an average not more than one-fifth of the nominal capital stock, which was far below what the law permitted.

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In New York, in 1832, the banks could issue nearly four times the amount which they actually put in circulation.^a According to Gallatin, writing in 1831, the average amount of notes issued by all the State banks in the country did not exceed 81 per cent of the capital.

Sudden or wide fluctuations in the volume of currency were generally regarded with concern, for the relation of note issue to the elastic demands of commerce and industry was but little recognized. Note issues were rather regarded as a medium of exchange, convenient and cheap, and therefore serviceable to the public; notes economized capital and facilitated the operations of business, and any marked change in the volume was held responsible for changes in prices. It was held, therefore, that the control of the currency ought never to be intrusted to individuals who could change the volume according to their own private interests; as well might individuals claim to be chartered for military purposes or for laying out turnpike roads.^b

VIII. DENOMINATIONS OF NOTES.

Limitations or restrictions directed against the issue of bank notes of small denominations were enacted in some of the States at an early date. Although a consistent policy was not adhered to, the agitation for the suppression of such notes continued to spread and occupied no small part in banking controversies as long as state bank issues prevailed. Arguments for their issue were obvious.

^a Report of Bank Commissioners, New York, 1832.

^b Report of Benjamin Hazard's Committee, Rhode Island, 1826.

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There was scarcity of specie, and it was urged that there was frequent need for the remission of sums under \$5. Moreover much of the country produce was purchased by dealers who traveled through the country and paid out small sums, and for these, it would be inconvenient to carry a large bulk of specie. Banks also found it for their interest to circulate the smaller notes which were less likely to come back for redemption. The disadvantages were not so apparent, but objection to their issue was found in the ease with which notes could be counterfeited, and the consequent hardship if circulated among the more ignorant and poorer classes. Again, they gave speculative banks a greater opportunity to inflate their issues.

The history of small-note issues conveniently divides itself into two periods before and after 1830.

The charter of the Massachusetts Bank, 1784, contained no express power to issue bills and consequently is silent as to the denominations of notes, but the validity of its notes was recognized by subsequent statutes. The issues of the Union Bank in 1792 were restricted to notes of \$5 and upward; those of the Nantucket and Merri-mac banks, next incorporated in 1795, to bills of \$2 and upward; and those of the Rutland and Essex banks, incorporated in 1799, to bills of \$5 and upward. In the same year the issue of bills under \$5 was prohibited to all banks, except the Nantucket. In 1802 the circulation of bills below that denomination, issued in other States, was prohibited under a penalty; this resulted in a scarcity of small change for currency, and in 1805 permission was given to her own banks to issue notes

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for \$1, \$2, and \$3 up to 5 per cent of the capital.^a This amount was increased in 1809 to 15 per cent.^b In 1812 it was reduced to 10 per cent,^c and in 1818 increased to 25 per cent, where it remained for many years.^d

In the other New England States there was less agitation, and in New York small notes were tolerated almost without dissent. New Jersey in 1812 attempted to establish a limit of \$3, but in the following year fell back to \$1, and in 1815 authorized her banks to issue notes for even less than \$1, pending the war with Great Britain. In 1830 the circulation of foreign bank notes under \$5, except those of New York City, were prohibited. This law, however, became a dead letter.^e

In Pennsylvania there was more decided opposition, and restrictions were imposed in 1817. There were, however, evasions of the law and many small notes were introduced from other States. Public sentiment was averse to stringent measures, and in 1820 defeated a bill prohibiting the circulation of foreign notes.^f Finally, in 1828, circulation of small notes of other States was prohibited. In Maryland specific prohibitions were inserted in the charters of the Bank of Baltimore, 1795, and the Mechanics' Bank, 1806, against the issue of notes under \$5; and in 1812 the restrictions were made absolute for all banks seeking a renewal of charter.

^aActs, Mass., 1805, ch. 24; Tenth Report of Bank Commissioners, 1860, p. 132.

^bActs, Mass., 1809, ch. 99.

^cActs, Mass., 1812, ch. 56.

^dActs, Mass., 1818, ch. 76; see also Root, Sound Currency, 2:4.

^eNiles, 47:176.

^fRaguet, Currency and Banking, p. 136.

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The suspension of specie payments in 1814, in this State as in other sections, delayed the progress which was being made toward the suppression of small notes. With the disappearance of specie, notes were issued in some States as low as 25 cents, some with the sanction of the law, and others without it. Notes were also issued by corporations, public officers, and individuals as low as 5 cents. It was difficult consequently, when specie payments were renewed, to regain the ground lost during the period of vitiated currency. Maryland, therefore, in 1814 was forced to make some temporary concessions, but when the war was over, endeavored to rid herself of these small notes. In 1820 the presidents of the Baltimore banks resolved that they would not issue any notes less than \$5.^a In 1821 the legislature, noting that the existing law was violated, imposed a penalty for each offense of issue by a bank, including a fine of \$5 to be paid by an individual for passing the note of any bank not chartered by Maryland.^b Such restrictions were not altogether welcomed even by bank critics. Niles, who frequently referred to small notes as "filthy dowlass," thought that public convenience would be served if one of the banks was authorized to issue \$3 notes,^c and in 1833, noting that bills under \$5 did not circulate in Maryland, remarks that it was necessary to carry about silver dollars and smaller coin, an inconvenience which hardly repaid for the security against fraudulent issues of \$1 and \$2 notes.^d Notwith-

^a Niles, 19:17.

^b Laws, Md., session of 1820, ch. 150; Niles, 19:417.

^c Niles, 29:177; November 19, 1825.

^d Niles, 45:145.

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standing this restrictive legislation, some of the country banks issued, contrary to law, small notes on the ground of necessity. Some, indeed, claimed the right as derived from their charters, which could not be impaired by subsequent legislation.^a

The legislature of Virginia in the charter of the Bank of Alexandria, 1792, forbade the issue of notes of less than \$5;^b and the same restriction is to be found in the charter of the Bank of Virginia, 1804. In 1815 some of the banks were authorized to issue notes for \$1, \$2, and \$3 until six months after the termination of the war with Great Britain.^c In 1816 it was enacted that no corporation or individual should issue a note or check for less than \$1, and the holder of such a note might recover \$5 against the maker.^d Virginia, like Maryland, suffered from small notes put into circulation by banks in the District of Columbia; although under the jurisdiction of Congress they were among the worst offenders and found a large field for profitable operations in spreading their circulation over neighboring States. It was consequently proposed that the Government prohibit the receipt of notes of banks issuing notes of less than \$5. Niles, however, who could not be regarded in any way as a bank sympathizer, questioned the expediency of legislating upon this subject; "for public opinion," he wrote, "was whipping the small notes out of circulation

^a Report of Bank Commissioners, Maryland, 1837.

^b Laws, Va., ch. 76, sec. 14.

^c Acts, Va., 1815, ch. 25.

^d Laws of Virginia, 1816, ch. 23, sec. 10.

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as rapidly as public convenience would admit."^a In 1820 Virginia enacted more stringent legislation, making the issue of notes or checks intended to be circulated as money for an amount less than \$5 a misdemeanor and punishable by fine or imprisonment. Penalties were also enacted against bringing such currency into the State with intent to circulate.^b In 1837 the prohibition was extended to notes of less than \$10, and after 1840 to notes of less than \$20.^c South Carolina, in 1812, forbade the Bank of the State of South Carolina to issue any note under \$1, and in the following year it forbade all other banks to issue notes under \$5, thus giving the Bank of the State of South Carolina the monopoly of the smaller notes. Ohio in 1819, Florida in 1828, and Georgia in 1830 forbade the issue of notes under \$1.

By 1830 there were then only three States—Pennsylvania, Maryland, and Virginia—in which notes under \$5 did not circulate. In North Carolina and South Carolina, and in a few other sections, there were notes as low as \$0.25, \$0.12½, and \$.06¼.^d The total amount of notes under \$5 in use throughout the country at this period was estimated at about \$7,000,000, and of \$5 notes at \$10,000,000.^e The agitation still continued, being reinforced by the hard-money policy of Jackson and those who desired to exclude all forms of paper money. In 1835 the Treasury Department began to exert pressure to reduce the circulation of bills of small denominations.

^a Niles, 19:298; Jan. 6, 1820.

^b Laws, Va., 1820, ch. 8, sec. 1-4; Niles, 19:65.

^c Laws, Va., 1836-37, ch. 82, sec. 1.

^d Gouge, *History of Paper Money and Banking in the U. S.*, pt. I, p. 56.

^e White's Report, Feb., 1831.

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A circular was issued (April 6) stating that the Treasury would exercise its discretionary power over the receipt of public money and that ultimately it intended to exclude all notes of a denomination of less than \$10. It, however, announced that it intended to make arrangements as soon as possible to discontinue the use of any bank as a fiscal agent which continued to issue notes less than \$5.^a Gallatin, although a friend of banks, advised the elimination of all notes under \$10.

Connecticut, in 1835, forbade the issue of notes of less than \$2, and of less than \$3 after January 1, 1836; in the next year the minimum was fixed at \$5. Her bank commissioners, however, in 1837, complained that \$1 and \$2 bills of Massachusetts and Rhode Island banks came in and in some sections were abundant. Such bills, in particular, were loaned by banks of Rhode Island and used by manufacturers for the payment of laborers; and as Connecticut banks would not receive them and prosecuting officers were averse to taking action, they remained in circulation.^b Maine, also, in 1835, passed an act prohibiting the circulation of all bills under \$5; no bank was permitted to issue any bills of \$1, and after January 1, 1836, no bills of \$2; and after June 1, 1836, no bills of \$3; and for the circulation of such bills there was a penalty of double the value of the bills to be forfeited. Two years later the commissioners reported that the law had been obeyed by the banks, but private individuals had encouraged the use of these illegal notes.

^a See also circular of Feb. 22, 1836.

^b Report of Bank Commissioners, Conn., 1837.

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The decisive action on the part of Pennsylvania in 1828 gave rise to a movement for a suppression in New York, and in 1835 (April 20) the legislature prohibited the circulation within that State of the notes of other States of a less denomination than \$5, the penalty being the forfeiture of the "nominal amount of such bank note, bill, or promissory note, with costs of suits;" and on March 31, 1835, an act was passed making it unlawful "for any person or corporation to pay, give, or offer in payment, or in any way circulate or attempt to circulate as money within this State, of a less denomination than \$5, or of a denomination between \$5 and \$10;" the penalty for violation of the act being four times the nominal value of such bill, note, or evidence of debt. Corporations having banking powers were also prohibited from issuing or putting in circulation notes of a less denomination than \$5, under a penalty of \$100 for each bill put in circulation. This act was superseded by the act of February 28, 1838, which contained still more stringent provisions against the issue and circulation of notes below the denomination of \$5.^a It proved difficult, however, to exclude outside bills, for on the northern frontier Canadian bills circulated quite as freely as those of New York banks. This was attributed to the defect in the laws which imposed a penalty upon both the person passing and the person receiving a note, thereby making it to the interest of both to conceal. The small note law was also evaded in instances by the use of small checks drawn by individuals upon a neighboring bank.^b

^a Assembly Report, N. Y., No. 215, March 2, 1835; Sen. Report, No. 108, March 25, 1834; Sen. Report, No. 10, Jan. 10, 1838; Niles, 48:158; 49:2.

^b Reports of Bank Commissioners, N. Y., 1837, 1838.

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So strong was the opposition to these restrictions that the question became an issue in the state election of 1838, and as a result the acts were repealed February 21, 1839.^a

Pennsylvania, in granting a state charter to the United States Bank in 1836, forbade the issue of notes under \$10; North Carolina, in 1833, established \$3 as the minimum limit; Georgia, in the same year, suppressed notes under \$5; and Alabama about the same time prohibited the circulation of notes of foreign banks under \$5.^b

Ohio, in 1836, also passed a restrictive measure, which was opposed by the banks on the ground that under their charters they possessed vested rights which could not be impaired. The legislature, therefore, tried an indirect method of compulsion by imposing a tax of 20 per cent on dividends, unless banks surrendered their asserted rights. The charter of the State Bank of Indiana, 1834, excluded notes of less than \$5, and the legislature reserved the right after ten years to prohibit notes under \$10. The Bank of Missouri, chartered in 1836, went even further and prohibited notes under \$20.

The suspension of specie payments in 1837, again retarded the movement for suppression. Small notes and tickets were once more brought into circulation, and many of the States legalized their use temporarily. A few banks in Massachusetts resorted to the issue of fractional bills for \$0.25, \$1.50, and \$1.75. Although the associated banks of Boston discountenanced these issues as contrary to the spirit of bank charters, public sentiment upheld the fractional bill banks as benefactors. New Jersey, in 1838,

^a Report of Comptroller of Currency, 1874, p. xxviii.

^b Niles 47:428.

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repealed an anti-small-note law passed in 1835. In 1837 Virginia suspended the small-note law until April 1, 1839, and expressly authorized the issue of \$1 and \$2 notes, not exceeding 4 per cent of the capital.^a This temporary permission was continued in 1840.^b In 1840 Pennsylvania and the Southern States were practically the only sections which were free from notes under \$5, and De Grand, in 1841, stated that the attempt to suppress the circulation of small bank notes had generally been repudiated by public opinion.^c

Agitation was renewed, however, beginning with about 1840, but so much ground had been lost that it was difficult to make much headway. In New York, enactments against circulation did not prevent the issue of notes, and in 1855, the small-bill law, which had been enacted twenty years before, was repealed on account of its nonenforcement. In 1860 New York was flooded with \$1, \$2, \$3, and \$4 notes of the banks in the interior and of the New England States. In Massachusetts an earnest effort was made in 1855 to suppress bills under \$5, but the country banks opposed and the legislature did not take action, for it was thought impossible to keep out the issues of other States.^d In Rhode Island fractional bills were prohibited in 1853; and at that time more than one-fourth of the total circulation of \$5,000,000 was in denominations under \$5.

^a Laws, Va., 1837-38, ch. 104; ch. 106, sec. 6.

^b Laws, Va., 1840-41, ch. 76; Laws, 1841-42, ch. 105.

^c Proceedings of the Friends of the National Bank, Boston, July 15, 1841, p. 15.

^d Tenth Report of Bank Commissioners, Mass., 1860, p. 129; Merchants Mag., 34:695.

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Pennsylvania again in 1850 (April 16) prohibited the issue of notes of a denomination less than \$5, but in another later act (April 17, 1861) authorized the issuing of notes of denominations of \$1, \$2, and \$3 to an amount not exceeding 20 per cent of the capital stock paid in.

Virginia in 1854 imposed a fine of \$10 for the issue of notes of less than \$5. The State constitution of Florida in 1845 forbade the issue of notes under \$5, and authorized the legislature, at its discretion, to raise the amount to \$20. The banking act of Ohio, 1845, provided that \$1 notes should not exceed 10 per cent; \$2 notes, 5 per cent; \$3 notes, 10 per cent, of the total circulation, and in 1854 the circulation of foreign bank bills of less than \$10 was prohibited. Indiana in 1855 forbade the State Bank of Indiana to issue more than one-twentieth of its bill circulation in denominations under \$5, and Tennessee placed a similar restriction upon banks other than the Bank of Tennessee.^a Kentucky in 1843^b restored the privilege of issue of notes of less denomination than \$5, but again imposed restrictions in 1858.^c

IX. REDEMPTION OF BILLS—LEGAL PENALTIES.

In the earliest charters there was no express provision made for the redemption of notes, nor was there any penalty for nonredemption. The issuing of notes was generally regarded as the principal object of a bank's existence, instead of an incidental function. The limitation of note issues to a certain proportion of the capital,

^a Merchants' Mag., 37:219.

^b See acts of March 8, 1843, and January 21, 1848.

^c Act of February 15, 1858.

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which was often represented by stock notes of shareholders rather than by solid funds, was of little consequence. Practically the only security for convertibility lay in the liability imposed upon stockholders, and more particularly upon directors, in case of failure or mismanagement. Indeed, many in the earlier part of the century considered that it was improper and injurious to call upon a bank for specie in payment of its bills. "Brokers who sent home the bills of country banks were denounced as speculators and bloodsuckers, whose extirpation would be a public benefit." Respectable men defended the conduct of banks in interposing obstacles to the payment of their notes to brokers who had bought them up to discount. A Boston broker was brought before the grand jury of Vermont for demanding payment in specie for the bills of one of its banks, on the complaint of the attorney-general that he was guilty of an indictable offense.^a

As a result of disastrous experience, various methods were tried to enforce redemption. On the one hand, the public, through its legislatures, imposed penalties upon banks for failure to honor their note obligations; and, on the other hand, prudent and well-managed banks found it necessary, in self-defense and for their mutual benefit, to establish voluntary arrangements whereby notes could be promptly redeemed. In Connecticut there was a somewhat unusual provision that in case of the failure of a bank the holders of notes of denominations less than \$100 should have a first lien upon all the assets of the bank. The note holder's priority was also recognized

^a Appleton, *An Examination of the Banking System of Massachusetts*, 1831, p. 4.

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by Ohio in 1845, by New York in 1846, and by Massachusetts in 1849.^a The legal penalties devised were of two kinds: first, a pecuniary fine for nonpayment; and, second, forfeiture of charter. The voluntary settlements are represented by such schemes as the Suffolk system in England and the practice in New York of redeeming country notes by responsible agents at a stated discount.

Massachusetts in 1810 took the lead in developing stricter responsibility by imposing a penalty of 2 per cent a month for failure to redeem notes on presentation.^b The suspension of specie payments during the years 1814-1816 naturally gave new importance to the subject of redemption, and at the close of the period, when the country endeavored to extricate itself from the embarrassment of a depreciated currency more wide-spread efforts were made to control bank circulation. The Second Bank of the United States, which received its charter from Congress in 1816, was required to redeem its notes as well as its obligations to depositors, under penalty of payment of 12 per cent interest during the period of nonfulfillment. New York adopted this principle, and many States in different parts of the country quickly followed.

New Jersey in a charter of 1823 prohibited a bank, upon failure to redeem notes in specie, from continuing to do business until resumption; and also provided for 10 per cent damages per annum. The same provisions were repeated in charters of 1824. A charter of 1828 provided

^a R. M. Breckinridge, *Jour. of Pol. Econ.*, March, 1899, p. 258.

^b Acts, Mass., 1810, ch. 37.

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for the forfeiture of charter and also for 10 per cent damages. In 1834 a charter provided for forfeiture if there was suspension for a space of seven days, but in 1837 this delay was increased to fifteen days.

In Maryland the charter of the Frederick County Bank, 1817, provided that if the bank refused to pay specie the charter should be null and void; in 1819^a the payment of 6 per cent interest on dishonored notes was enacted for all banks, a rate which was quickly raised to 12. In Pennsylvania, in 1824, the cashier was required to indorse a note when refused and the payment of dividends was forbidden during the suspension.^b

With few exceptions previous to 1830 there were no penalties in southern charters for not redeeming notes. Banks were under no legal obligation to pay demands except by suit, and note holders were in the same position as other creditors. Virginia, in 1834, made the Merchants' and Mechanics' Bank liable for 12 per cent interest besides damages, and in 1837, by general statute, made failure to pay in specie a ground for issuing judgment on ten days' notice for the amount of the bill and 10 per cent damages and 15 per cent interest. It also provided for forfeiture of the charter.^c In 1838 the penalties were temporarily waived, and in 1841 that of forfeiture of charter was repealed.^d It was then provided that notes presented and not paid in specie should be indorsed by the cashier and be subjected to 6 per cent interest. In 1856^e the rate was

^a Laws, Md., session of 1818, ch. 117; Niles 16:359.

^b Acts, Pa., March 25, 1824.

^c Laws, Va., 1836-37, ch. 82, secs. 4, 5.

^d Laws, Va., 1840-41, ch. 77, secs. 2, 3.

^e Laws, Va., 1855-56, ch. 79, sec. 19.

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raised to 12 per cent. In North Carolina a charter was granted in 1833 which included a penalty of 12 per cent interest in case of refusal to redeem; and in South Carolina, in 1840, it was enacted that in case of nonredemption of notes, the bank should pay 5 per cent of its circulation every month. Florida imposed a penalty for nonredemption, in some instances providing for 10 or 12 per cent damages, and in others demanding a forfeiture of charter. In case of suspension by the Bank of Florida, 1843, the directors were liable to indictment for misdemeanor, and on conviction, to imprisonment for five years and a fine of \$5,000, the president and cashier were liable for indictment for felony and to imprisonment for five years and a fine of \$20,000, and in addition the bank was called upon to pay 5 per cent damages.^a Alabama, in 1821, passed an act providing that nonspecie paying banks should show cause why their charters should not be revoked. Charters of most of the banks in Louisiana, down to 1837, contained an express condition of forfeiture for failure to redeem.^b

In Ohio, by the general law of 1824, suspended banks were subjected to interest on notes demanded and not paid, but were exempt from further interest by giving notice of the time they would resume. In charters from 1829, with one exception, a penalty of 12 per cent in addition to legal interest was imposed. In the charters granted in 1833-34 the legislature reserved in case of nonredemption the power to amend or repeal the charter. In

^a Acts, Fla., March 5, 1843.

^b See Governor's Message, La., December 11, 1837.

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one case suspension for more than thirty days was expressly made a forfeiture.

Kentucky, in 1818, by a law creating forty new banks, enacted that all notes should be redeemed either in specie or in notes of the United States Bank, or of the Bank of Kentucky; if refused, charters would be liable to forfeiture. In 1821 Kentucky intentionally adopted a policy of inflation and the Bank of the Commonwealth by its charter "was relieved from all danger of suspension by not being required to redeem its notes in specie. Its paper was made payable and receivable in the public debts and taxes, and certain lands owned by the State south of the Tennessee River were pledged for the final redemption of its notes." The charter of the Louisville Bank of Kentucky, 1833, made it unlawful for the bank to issue any note, bill, or to loan money after it shall have failed to redeem its bills or notes in specie.

Indiana, in 1818, provided that if a bank failed to pay notes in specie the cashier should be required to indorse that fact on the note, after which the note should draw interest at 6 per cent; in 1834, 12 per cent interest was allowed and suspension constituted grounds for closing the bank as insolvent. The charter of the State Bank of Indiana, 1842, provided that failure to pay in specie was a cause for closing the bank except when the specie was demanded by nonspecie paying banks in Ohio, Illinois, Kentucky, or Michigan, or by those intending to send the specie out of the State.^a

^a Laws, Ind., 1842, ch. 68, sec. 7.

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Illinois, in 1816, in granting a charter to the Bank of Illinois at Shawneetown, fixed the penalty for suspension at 12 per cent, but in 1841 the State Bank of Illinois complained that it was the only bank in the State whereby suspension involved a forfeiture of charter. Missouri, in chartering the Bank of Missouri, the second bank in the State, required that all notes should be redeemed under penalty of a forfeiture of 5 per cent per month.

X. REDEMPTION BY VOLUNTARY SYSTEMS.

Early in the century the question of accepting bank notes in all places at par became a subject of dispute. Banks in the Eastern States rapidly increased, and they wished to gain all possible advantage from the circulation of their notes in Boston. Objection was then made to the cost of guaranteeing redemption because of the expense of transportation, and this was entirely apart from any suspicion of a bank's ability to redeem. Practice varied; sometimes the bills were received at a distance at par, sometimes at a small discount. "The country banks considered it a great hardship that the Boston banks should send home their bills and demand specie for them instead of putting them in circulation again. Public opinion took the side of the country banks, and the Boston banks very unadvisedly gave up receiving the bills of out-of-town banks altogether. The consequence was that the bills of country banks obtained the entire circulation even in Boston. Boston banks had given them currency, their solvency was not doubted, and for all common purposes they became equally current with the bills of the Boston

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banks, which were only necessary for the purpose of making payments at those banks. A double currency was thus introduced; the one called foreign money or current money; the other, Boston money, the difference being for several years about 1 per cent. * * * This state of things introduced a new branch of business and a new set of men, that of money brokers, whose business it was to exchange these currencies one for the other, reserving to themselves a commission of about one-fourth of 1 per cent or, in the language of the day, giving a premium of three-fourths per cent for Boston money and selling it at a premium of 1 per cent. * * * The supply ere long of (foreign) money exceeded the demand; and as the channels of circulation overflowed, the brokers began to send the bills home for payment. The state of the currency became the subject of general complaint. The brokers were denounced as the authors of the mischief and the country banks made no scruple of throwing every obstacle in the way of their operations. * * * It was soon discovered that a bank could be made profitable in proportion to its distance from Boston and the difficulty of access to it. The establishment of distant banks became a matter of speculation, the favorite locations being the remote parts of Maine and New Hampshire."^a

An organized effort was then made to extend the circulation of foreign bank notes by the incorporation, in 1804, of the Boston Exchange Office. This had a capital of \$150,000, consisting of foreign money and \$50,000 in specie. The charter provided that the corporation should

^a Examination of the Banking System of Massachusetts, 1831, pp. 10-12.

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not make any demand for specie in any other incorporated banks "whereby to cause distress, nor offer to furnish any person or persons with bills to that purpose;" and the office in turn was restricted from asking or receiving a premium for exchanging bills of any bank for specie, or from purchasing a bank's bill at a discount. This institution, however, was bought up by a promoter who used it for speculative purposes, and the experiment did not receive a fair test.

As the evils of a depreciated currency increased, the merchants of Boston in 1808 formed an association for the purpose of sending back bank notes and demanding specie for them. "This soon brought the currency to a crisis. The Farmers' Exchange Bank in Rhode Island suddenly failed under the most alarming circumstances. The shock upon the public was tremendous. The Berkshire Bank soon followed. The discovery that banks could fail affected the credit of all. In the course of the year 1809 the greater part of the country banks of Massachusetts, Maine, and New Hampshire having any considerable amount of bills in circulation stopped payment."^a

It was at this time that the legislature of Massachusetts imposed a penalty for nonredemption. But more supervision was needed than could be obtained by statute. Foreign bank bills flowed into Boston to excess, and these could not be converted into Boston funds except at a discount from 1 to 5 per cent. It was estimated that the exchange of bills reached \$100,000 a day, with an annual

^a Appleton, *Examination*, etc., p. 14.

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cost to note holders of \$125,000. Country banks "stuffed the money market everywhere with their paper."^a

In 1814 the New England Bank in Boston individually undertook the task of securing the redemption of bills of New England banks. It received the notes of all these banks at a discount varying according to distance, but in no case exceeding 1 per cent; and on condition of a permanent deposit they were returned to the issuing bank at the same rate of discount. Discounts were thus kept within a range of one-fourth to three-fourths per cent. This policy tended to reduce the circulation of outside banks.

XI. SUFFOLK SYSTEM.

In 1819 the Suffolk Bank, of Boston, determined to undertake the redemption of foreign money according to the terms adopted by the New England Bank. It was voted that any bank placing with the Suffolk Bank \$5,000 as a permanent deposit, with such further sums as would be sufficient to redeem its bills taken by the Suffolk Bank, should have the privilege of receiving its own bills at the same discount at which they were purchased. Banks in Providence and Newport and 23 other banks, then keeping an account with the Suffolk, were excepted from the requirement of a permanent deposit of \$5,000, provided they made all their deposits at the Suffolk Bank. If any bank refused to make the deposit required, its bills should be sent home for payment. As a consequence of the competition of the Suffolk Bank with the New England Bank, discount on

^a Hazard's Committee, Rhode Island, 1826.

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country bank notes was lessened; but "the animosity of the country banks, which were unwilling to keep a deposit in Boston for the redemption of their bills, was naturally very much aroused when the Suffolk Bank, collecting their bills, sent them home for specie, and much ill feeling was engendered."^a Various devices were planned to thwart the efforts of the Suffolk Bank. When the Lincoln Bank, in Wiscasset, was called upon for redemption of \$3,000 of its notes, its office first tendered a Boston draft, which was declined. The cashier then sought delay by delivering small change, and by the hour of closing the doors had counted out only \$500 in coins, nothing larger than 25 cents.^b

Owing to the monopoly which the country banks still possessed in the note circulation of Boston, it was determined to take more decisive action, for though Boston had more than one-half of the banking capital of New England it supplied only one twenty-fifth of the bills in use.^c The Suffolk Bank consequently addressed a letter, April 10, 1824, to each of the Boston banks, calling attention to the fact that the "prodigious credit thus enjoyed by the country banks is not owing to any superior confidence in the stability of these institutions or in their ability to redeem their promises in gold and silver, but may be attributed to a discount founded on the very difficulty and uncertainty of means of enforcing this payment. Such would not be the natural operation of these causes were these institutions what they professed to

^a Whitney, *The Suffolk Bank*, p. 9.

^b Niles, June 16, 1821.

^c Whitney, *The Suffolk Bank*, p. 10.

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be, establishments for the discount of country notes and the convenience of country traders. Their bills would then circulate only in their own immediate vicinity. * * * Under the existing circumstances, we presume that a very great proportion of the discounts of the country banks are made in Boston. Loans to an immense amount are made by their agents here at reduced rates of interest, payable in three or five days after demand, so that they can be in funds at very short notice, and in this manner necessarily deprive us of much valuable business. And this great circulation is enjoyed by the banks out of the State, who do not pay the tax to the Commonwealth which we are compelled to pay.”^a Attention was also called to the successful practice of New York banks, which, though they deducted no discount to reimburse them for the expense of sending bills home for redemption, found a compensating profit in the increased circulation of city notes. The Suffolk Bank thought that a discount of only one-fourth of 1 per cent would be required if it should undertake the work of redemption. It was, therefore, proposed that a fund be assessed upon the banks in proportion to their respective capitals, to be placed at the disposal of one or more banks for the purpose of sending home the bills of the banks in Maine.

At a conference which was held of representatives of the Boston city banks it was voted expedient to send home the bills of all banks out of the State and also the bills of other banks, as might be determined upon. Seven banks thereupon subscribed \$300,000 in order to carry out the

^a Whitney, *The Suffolk Bank*, 12-13.

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arrangement, and the Suffolk Bank was chosen as the agent.

This action created much excitement. The country banks realized that they must curtail their circulation and that it would probably be necessary to keep a larger specie reserve.^a For a brief time there was a bank war directed against what was called the "Holy Alliance" and the "Six-Tailed Bashaw." Some of the oldest and strongest country banks held out for a considerable period, refused to deposit, and paid in specie all demands.^b

The Hartford Bank, for example, claimed that the system was arbitrary and unjust and needlessly curtailed the profits of circulation.^c The Worcester Bank, which kept its deposit with the New England Bank, also declined the proposals of the Suffolk Bank and declared that it would not consent to negotiate under an attempt at coercion.^d A messenger from the Suffolk Bank presented \$38,000 of the Worcester bills, or more than one-half of its circulation; the Worcester Bank, having a credit of \$39,000 with the New England Bank, tendered a draft in payment, which the messenger agreed to accept if the Worcester Bank would keep its deposit with the Suffolk Bank. This offer was refused and the Worcester Bank paid \$28,000 in specie and dispatched a messenger to Boston to pay the balance over the Suffolk's counter. The Suffolk Bank, however, declined the tender and sent a sheriff to attach real estate of the Worcester Bank.

^a Whitney, *The Suffolk Bank*, p. 15.

^b Niles, May 14, August 27, 1825.

^c Woodward, *The Hartford Bank*, p. 130.

^d Worcester Bank, p. 14; July 26, 1826.

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In 1825 the system was modified so that country money was received at par, instead of at a discount. Under these terms, the business of the Suffolk Bank rapidly developed and finally all of the banks in New England practically accepted the arrangement. "The general arrangement was as follows: Each bank placed a permanent deposit with the Suffolk Bank of \$2,000 and upwards, free of interest, the amount depending upon the capital and business of the bank. This sum was the minimum for banks with a capital of \$100,000 and under. In consideration of such deposit, the Suffolk Bank redeemed all the bills of that bank which might come to it from any source, charging the redeemed bills to the issuing bank once a week or whenever they amounted to a certain fixed sum, provided the bank kept a sufficient amount of funds to its credit independent of the permanent deposit to redeem all its bills which might come into the possession of the Suffolk Bank. The latter bank charging it interest whenever the amount redeemed should exceed the funds to its credit; and if at any time the excess should be greater than the permanent deposit, the Suffolk Bank reserved the right of sending home the bills for specie redemption. As soon as the bills of any bank were charged to it, they were packed up as a special deposit and held at the risk and subject to the order of the bank issuing them. In payment the Suffolk Bank received from any of the New England banks with which it had opened an account the bills of any New England bank in good standing at par, placing them to the credit of the bank sending them on the day following their

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receipt.”^a In 1831 the banks were charged daily with all their redeemed bills instead of weekly. In 1834 the business of redemption had increased to such an extent that it was difficult to assort the bills in time for the daily settlement. The Suffolk Bank therefore notified the Boston banks that instead of receiving all their foreign money at par, it could take on any one day only an amount equal to one-half of their permanent deposit. Above that proportion it would charge one-tenth of 1 per cent. It also restricted the foreign money to that received in the regular course, excluding deposits from banks and brokers.^b

“The banks of New England were divided into two classes—those keeping a deposit with the Suffolk Bank and redeeming their bills at its counter; and those which kept an account with some other Boston bank, with which an arrangement was made for the redemption of their bills. The Suffolk Bank did not require the New England banks to keep a deposit with it as a condition precedent to receiving their bills at par. On the contrary, it received at par the bills of all sound New England banks, whether they kept an account with it or not. It only required that they should redeem their bills at some convenient place on penalty of having them sent home for specie.

“For the bills of the former class of banks the Suffolk had security in the form of deposits and collections. For the bills of the other class it had no security except the good faith of the banks acting as their agents, and

^a Whitney, *The Suffolk Bank*, pp. 19-20.

^b *Ibid.*, p. 24.

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to which it charged and sent daily all the bills for the redemption of which they were responsible. As these could not be sent till the day after they were received, the Suffolk Bank was actually taking the risk of redemption on all this class of bills for one day without any security; and should any of these banks fail it had no positive assurance that the redeeming bank, with which such failed bank kept an account, would receive from it the bills it might have in hand.”^a

During the earlier years of the system the Suffolk Bank had much difficulty in securing adequate deposits to meet the terms of agreement with the banks. Particularly was this so after 1831. Between that year and 1833, 90 new banks were chartered in New England, of which 45 were located in Massachusetts. “The Suffolk Bank became overloaded with redeemed bills; the banks were slow in making remittances and the accounts of many of them were overdrawn.” The Suffolk Bank thereupon notified the banks which had overdrawn that their drafts would not be allowed above \$10,000. Notwithstanding these instructions, 44 banks, in 1836, had overdrawn \$664,000.^b

After the suspension of specie payments, in 1837, the Suffolk Bank was not in a position to coerce the other banks. Some of these continued to redeem at the Suffolk, while others withdrew their accounts. Moreover, the Suffolk Bank was unable to reduce the overdrafts of some of its correspondents, particularly in Maine, and it was finally obliged to decline to receive the bills of a large

^a Whitney, *The Suffolk Bank*, p. 46.

^b *Ibid.*, 23-25.

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part of them. Notwithstanding these difficulties, the system was continued after resumption took place.

In Rhode Island the Merchants' Bank of Providence became the agent of the Suffolk. It made arrangements with most of the state banks to redeem for them the bills of all other banks except those of banks located in the same town. For this purpose it issued a large part of its circulation in the form of bills in denominations from \$100 to \$1,000, and had an understanding with other institutions that such bills, when received in the course of business, would not be presented for redemption in specie, but only in payment of their own notes. The Merchants' Bank thus refused to receive from any bank the bills of other banks in the same town, but left each to care for its own circulation by frequent redemptions of the bills of its immediate competitors, while it cared for the redemption of the banks by groups in each town. The Merchants' Bank paid interest on any balance against it, while the Suffolk Bank paid none.^a

The following table^b shows the redemptions which were made by the Suffolk Bank from 1834 to 1857:

1834 -----	\$76,000,000	1846 -----	\$142,000,000
1835 -----	96,000,000	1847 -----	165,000,000
1836 -----	127,000,000	1848 -----	178,000,000
1837 -----	105,000,000	1849 -----	199,000,000
1838 -----	77,000,000	1850 -----	221,000,000
1839 -----	107,000,000	1851 -----	243,000,000
1840 -----	94,000,000	1852 -----	245,000,000
1841 -----	109,000,000	1853 -----	288,000,000
1842 -----	106,000,000	1854 -----	231,000,000
1843 -----	104,000,000	1855 -----	341,000,000
1844 -----	126,000,000	1856 -----	397,000,000
1845 -----	138,000,000	1857 -----	376,000,000

^a Report of Bank Commissioners, Rhode Island, 1836.

^b For figures from 1834-1850, see Merchants' Mag., 25: 467; also Knox, History of Banking, p. 369.

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The total cost to the bank for carrying on this work of redemption in 1858 was \$40,000, or about 10 cents per \$1,000.

In 1837 it was estimated that two-thirds of the circulation of Connecticut was redeemed once in thirty days and the other third once in forty-five days, largely due to the redemption facilities in Boston and New York; in 1842 it was estimated that one-eighth of the circulation of the Connecticut banks was redeemed weekly at the Suffolk Bank; and in 1849 it was reported that Connecticut circulation was redeemed in Boston once in sixty days. In Maine, in 1842, a sum equal to the whole circulation of banks in that State was redeemed at the Suffolk Bank about five times a year; the average time which a bill issued by a Maine bank was in circulation until redemption was only about two months. In Rhode Island, toward the end of the system, there was a circulation of from \$3,500,000 to \$5,300,000, and the average local life of a bill was not over a fortnight. Taking the circulation of New England as a whole it was calculated that in 1857 it was redeemed eight times annually.^a

On the whole the system met with warm commendation on the part of the best bank and state officials who had charge of supervision. The bank commissioners of Connecticut, in 1842, expressed a general approval of the system; it checked excessive discounts and circulation. In Maine, the bank commissioners, in 1842, also stated that in their opinion the Suffolk system had preserved banks in Maine from the disasters which had occurred in some

^a Bankers' Mag., 12:70; White estimates it ten times a year, Money and Banking, p. 297.

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of the other States; the three banks in Maine which did not redeem their circulation in Boston, although sound, were not able to float their notes far from home: "Was there not a moral obligation resting on those banks to make their bills current in Boston, so as to prevent any public apprehension?" Again, in 1857, the commissioners referred to the great benefits derived from the Suffolk system; whatever objections there were to it in theory, its practical operation had kept the banks in good credit. A bank ceased to be in good standing when it was "thrown out of Suffolk."^a

The Suffolk Bank system, however, did not escape criticism. There was objection prompted by the selfish interest of foreign banks. The Suffolk Bank, it was declared, made New England pay tribute to Boston; it created a perpetual run of every country bank upon every other for the benefit of the Suffolk; it operated under "a higher law;" and it made New England helplessly dependent for currency at the feet of the banks at Boston. It was also argued that the system was a device for causing country bank notes to flow into Boston, and thus magnify the commercial prosperity of that city at the expense of the country. In reply, however, it was maintained that the influx of country bank notes was due to the concentration of trade and capital at Boston, and this rendered a system of par redemption necessary. It was also an advantage to a merchant in the interior who wished to purchase merchandise in Boston, for he could carry with him country bank bills without resorting to specie or the purchase

^a See also Report of Monetary Commission, p. 327.

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of a draft on Boston, for he knew that his bank bills were at par there.^a It was argued by some that the banks were not able to maintain as large a circulation as they would if the Suffolk system had not been in operation. When the plan was first introduced, there was truth in this claim; for example, the circulation of 16 banks in Massachusetts, in six months in 1825, was decreased \$382,000; in Maine there was a decrease in the same time of \$337,000; while the circulation of Boston banks increased \$283,000. According to Appleton,^b the principal inducement to the associated banks in Boston to appropriate the necessary funds to establish this system was the belief that the measure would increase their own circulation, but this effort in the course of a few years was partially defeated by the establishment of banks in the immediate vicinity of the city, as Charlestown, Cambridge, Roxbury. The real grievance, however, of many of the complaining banks was that their paper was raised to par value and they were deprived of profits previously made from depreciation.^c As the system developed, the notes of country banks were given a standing which they otherwise would not have obtained. When complaint was made in 1850 that the aggregate circulation of the Maine banks was one-fifth less than the limit fixed by law, it was urged in reply that country banks could float a circulation far greater in proportion to their capital than that of the Boston banks;^d for the latter

^a Merchants' Mag. 1851, 24:79.

^b Examination, etc., p. 18.

^c Hazard's Report, Rhode Island, 1826.

^d Merchants' Mag., 1851, 24:710.

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were by this system prevented from keeping a single dollar of their notes in circulation out of Boston, since the whole was gathered up by country banks and returned to Boston for redemption. The capital of thirty banks in Boston in 1850 was \$21,010,000; their circulation was \$6,070,000. The capital of Maine banks in the same year was \$3,148,000, while their circulation was \$2,301,000.

Critics argued that the conditions which the Suffolk Bank imposed upon its correspondents were too hard, but analysis made by a writer in the *Merchants' Magazine* controverts this claim; for example, a bank with a capital of \$100,000 was required to deposit in the Suffolk Bank \$3,000, the interest on which at 6 per cent per annum was \$180. A bank in Maine could circulate its bills to the amount of 75 per cent of its capital stock, but the average circulation of the sounder banks having a capital of \$100,000 did not exceed \$50,000. The average redemption by the Suffolk Bank of such an institution was about \$10,000 a month or \$120,000 a year. The bank was at the expense and risk of remitting this sum of \$120,000 every year in order to redeem its circulation, and this expense might be reckoned at one-fourth of 1 per cent, or \$300. Other expenses would add \$120 more, making the total cost of redeeming at the Suffolk Bank, \$600. On the other hand, the average rate of exchange between Boston and other places in New England was not less than one-half of 1 per cent, which would give \$600 on \$120,000.^a If, however, the circulation was redeemed more frequently the cost to the bank was greater.

^a *Merchants' Mag.*, 1841, 5:262.

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The criticism of Amasa Walker, writing in 1857, was more searching. He asserts that the system was begun on the right principle, but had not been carried out faithfully. It should have been recognized and regulated by law; returns should have been required of all moneys received of the several banks and the accounts with each bank. There was a common impression that the country banks had specie in the Suffolk with which to redeem their bills, but as a matter of fact there was no great reserve of specie in the Suffolk bank. It had in 1856 twice as much circulation as its specie; the specie reserve was a fiction. The arrangement by which the bank undertook to make the bills of all the New England banks current in Boston was a good one; it acted as a check on the operations of banks disposed to go to an excess, and it was a balance wheel to the dangerous system of currency. The idea of a deposit was a farce, however, for the Suffolk Bank loaned back money deposited with it to the bank from which it was received on condition of receiving interest, by allowing the depositing bank to withdraw its account to the amount of its deposit. In reality the Suffolk Bank was simply a great clearing house in which all the balances of New England banks outside of Boston were settled. It was a good regulator of a bad system.^a

Although the services of the Suffolk Bank and the system which it represented were approved by the soundest banking opinion, there was frequent friction, and about 1855 a movement was started on the part of

^a *Nature and Uses of Money and Mixed Currency*, pp. 65-67.

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outside banks to establish an institution of their own which should conduct the business of redemption. As a result, the Bank of Mutual Redemption was organized in 1856 on a coöperative plan. As originally designed, banks in Massachusetts were to subscribe one-half the capital of \$3,000,000, and banks in the other New England States the other half. In order to prevent any one bank or small group of banks from gaining control, it was provided that no bank could subscribe more than 5 per cent of its capital. In this way it was believed the foreign banks would be able to distribute back to themselves the profits which were derived from assorting country money.^a Within a year 143 banks held stock and the project proved successful.^b

Under these conditions the special influence of the Suffolk Bank came to an end.^c The principle, however, had been justified. "The bank had not labored in vain; it had found the currency of New England in a chaotic state, but by putting this principle into practice it had brought order out of confusion, and had compelled banks to keep themselves stronger than they otherwise would."^d Its successful operation was undoubtedly aided by a law passed by Massachusetts in 1845 forbidding any bank to issue any notes except its own, but yet it must be remembered that the system had been well tested long before that date. Other reasons for the successful working of the Suffolk system are to be found in the rigid system of

^a Bailey, *Bankers' Mag.*, 31:311.

^b *Bankers' Mag.*, 13:903.

^c *Bankers' Mag.*, 13:384-393; 21:964.

^d Whitney, *The Suffolk Bank*, p. 60.

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examination and supervision of banks by state officials which was early developed in nearly all parts of the New England States, and the fact that by allowing the correspondent banks to overdraw the Suffolk Bank could exert a powerful pressure. "The country banks kept their circulation as extended as possible for their own profit. Their overdrafts on the Suffolk enabled them to do so, but at the same time it put them completely into its power."^a

It must also be remembered that the operation of this system was confined to the area of New England, a section of homogeneous business interest, and there is grave reason to doubt if it could have been extended over the whole United States, limited as it was at that time.^b

XII. REDEMPTION IN NEW YORK.

The redemption of country notes in New York was undertaken in a less systematic way than that attempted in New England. Country banks, as a rule, did not keep specie in their vaults, but funds in the city banks, and redeemed their paper by drafts on the city. This redemption was interrupted in 1834, not because the country banks were unable to redeem, but because the city banks stopped taking up their notes. Some of the banks in Albany undertook the purchase of country bank notes at a moderate discount, and sent them home for redemption by a messenger.^c The act of May, 1837, which legalized suspension, provided, however, that during the suspension

^a Whitney, *The Suffolk Bank*, p. 37.

^b Report of Comptroller of Currency, 1878, p. xi.

^c Report of Bank Commissioners, New York, 1835.

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of specie payments each bank should receive the notes of other banks at par in payment of debts. When resumption took place, the city banks were averse to continuing this. A voluntary arrangement was consequently substituted, by which some of the city banks undertook to purchase country notes at one-half and then at three-fourths per cent discount, and to hold them until redeemed in funds current in New York City. Again, in turn, this arrangement was dropped, since it required more capital than the city banks wished to devote to it. By the next plan, the country banks made exchanges among themselves of each others' paper at the State Bank in Albany, but this provided no means of taking the notes out of New York City, and consequently their bills sold at a discount there. Objection was raised to a proposal that banks should be compelled to receive each others' notes at par, for, if this were done, country bank notes would engross the circulation in New York City. The safety-fund banks, however, by the act of 1829, were prohibited from purchasing their own notes at a discount, so that if they redeemed at all in New York they must redeem at par, but this did not apply to banks organized under the act of 1838. The buying of a bank's own notes, as well as those of the safety-fund banks, proved more profitable for the free banks than ordinary discount business, and tended to displace the notes of the safety-fund banks. This lessened the ability of the latter to discount. Free banks were doing a business in shaving notes of other banks.^a A compromise was sought in 1840, and (May 4) an act

^a Knox, History of Banking in the United States, p. 416.

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was passed requiring all banks outside of New York, Albany, and Brooklyn to appoint an agent who should keep an office either in New York or Albany for the redemption of circulating notes at a discount of not more than one-half of 1 per cent.^a This made the notes of a country bank in the more distant parts of the State more valuable as a medium than specie, for the discount was less than the expense of transportation.

A further step had already been taken by the banking law of April 18, 1838, which provided that it should not be lawful for any bank authorized under that act to issue any notes at less than \$1,000, to be put in circulation, payable at any other place than the bank's office. In 1844 it was proposed that banks be compelled to redeem in New York City, but a legislative committee reported adversely, on the ground that it necessitated a scattering of resources. It was held that the ability of a bank to redeem was not increased by taking funds out of its own vaults and intrusting them with a distant agent; such a measure would concentrate financial power in a few hands in the city of New York and make the country banks mere branches.^b

The bank commissioners in 1843 believed that the law of March 4, 1840, New York, requiring country banks to keep agents in New York and Albany for redemption of circulating notes had worked admirably in preserving uniformity in the rates of discount. Formerly it was not unusual to discredit the notes of sound institutions for the purpose of purchasing them in market, but the new law had checked

^a Report of the Bank Commissioners, New York, 1840; Assembly Report No. 325, April 21, 1840; Assembly Report No. 146, February 18, 1840.

^b Assembly Document, N. Y., No. 127, March 14, 1844.

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the establishment of associations at places remote and difficult of access, so as to render the transmission of the notes for redemption vexatious and expensive.^a

The comptroller of the State, however, in the next year, reported in opposition to this view. He thought that the redemption at a discount of one-half of 1 per cent was one of the principal inducements for establishing free banks; notes were signed and circulated in the city of New York; and by fixing the place of redemption at some distant point, the note holder was obliged to go to the office in Wall street, where the notes were really issued, and pay one-half of 1 per cent for redemption. It was therefore advocated that banks be required to redeem their notes at par in New York so as to reduce the motive for multiplying shaving shops. Again, in 1847, the comptroller advised par redemption. He believed the objection that banks would be compelled to redeem at two places was not sound; the practical effect would be redemption at only one place. As it was, banks were established in obscure places with the view of obtaining a circulation only and of doing no other business. In 1851, the act of 1840 was so amended as to reduce the discount upon country currency to one-fourth of 1 per cent. This act closed the door to illegitimate banking, and many institutions wound up their business.^b

^a Report of the Bank Commissioners, N. Y., 1843.

^b See Report of Comptroller of Currency, 1873, pp. xiv-xv.

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XIII. METHODS OF EVADING REDEMPTION.

During the first half of the century various devices were employed by speculative banks to increase their circulation and avoid redemption. In 1818, a legislative committee of New York enumerated some of the schemes which were thus adopted, such as placing a fund in a distant bank to redeem notes, and, after it became generally known that the notes were at par in that quarter, issuing a new emission signed in ink of a different shade, at the same time giving secret orders to the correspondent bank not to pay the notes thus signed. Others issued a species of paper called "facility" notes, not payable in money, but receivable by banks issuing them in payment of debts due. Again, large accommodations were given to individuals, on agreement that the borrowers should keep in circulation a certain sum for a specified time, the notes being designated by a private mark; and, in case the notes were returned before the date set, the borrowers were to be charged with the discount on such sum for the remainder of the period. To others, loans were made on condition that the borrowers pay their notes when due in what was called current money; that is, notes of banks which were current throughout the State, but not including the bank's own notes. The borrower, therefore, was often obliged to pay, as the time drew near, a premium in order to secure acceptable notes.

Most of these schemes bordered so closely upon fraud that they had to be abandoned. Other methods, how-

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ever, were employed, some of which may be enumerated as follows:

1. About 1835 it became common for banks in the North to employ agents to exchange bills of one bank for notes of other banks. This practice was continued in Massachusetts and complained of by the commissioners in a report of 1840. The bank inspector of Vermont, 1837, criticised the practice and characterized it as a kind of piracy of one bank on another; a bank situated within reach of other banks sometimes had to decide against discounting an application for a loan because of the belief that the bills would be circulated in the vicinity of an exchange agent and would be promptly taken up and sent back for redemption. This consequently forced banks to seek for discounts at distant places.

2. In some States, banks made their notes payable at some other place than where the office was located; for example, in 1816, the Dedham Bank of Massachusetts issued three-fourths of its circulation drawn on the cashier of the bank at Middletown, Connecticut. The legislature promptly passed an act prohibiting the issue of notes payable at other banks unless payable also at the bank of issue.^a This act, however, did not extend to checks or drafts for sums exceeding \$100, and it was subsequently learned that the Dedham Bank issued bills for \$101 in order to avoid the penalty.^b In the Southwest, this practice became an established custom. For example, the Union Bank of Tennessee, 1837, had in circulation \$1,598,000 payable at New Orleans, as well

^a Acts, Mass., 1816, ch. 91, May session, p. 345.

^b Resolves, 1819, ch. 254, p. 697.

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as a large amount payable at Philadelphia. The Bank of Illinois at Shawneetown, in the same year, had a considerable volume of notes payable at New Orleans, Louisville, and Philadelphia.

3. Notes were loaned on an agreement that they would not be presented for redemption within a certain time. In 1839 the bank commissioners of Massachusetts complained that some banks in that State loaned bills at a lower rate of interest on condition that they should be kept in circulation, or, in other words, that as often as the notes came home they would be redeemed by the borrower and again be put in circulation.^a In Connecticut the legislature in 1837 found it necessary to pass a law prohibiting banks from making loans which involved an express agreement that the notes would not be returned to the bank for redemption within a limited time. The practice still continued, for in 1853 the bank commissioners reported that some of the banks had engaged in loaning to persons outside the State, the borrowers guaranteeing redemption. These bills were so loaned that they could be readily detected at the counter of the bank, and were returned to the borrower, who redeemed them. This was called "protective circulation," and in that year amounted to \$1,353,000. As a result, the legislature in the following year forbade a bank to loan its bills to any other bank, in or out of the State, for circulation under an understanding or an agreement to keep them in circulation for a specified period, or of redeeming them if returned within a certain time.^a

^a Report of Bank Commissioners, Mass., 1839, p. 19.

^b Merchants' Mag., 31: 225.

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4. A most common method was putting notes in circulation at distant points. Its extreme form is to be found in the "Saddle-bag Bank" described by Niles in 1820: "A bank whose notes were carried about the country in saddlebags to be exchanged with landowners for their notes." In the middle of the century the practice was illustrated in the development of "Wildcat banks" in the West. But banks in the East were also guilty. Ill-managed banks supplied brokers, shopkeepers, tavern keepers, drivers, and workmen with quantities of paper and paid them liberally for getting it off. Agents carried these notes to every corner of the country, even to the British provinces, and beset travelers for an exchange of bills. One broker in Rhode Island put off in one year more than \$200,000 of the notes of a speculative bank, mostly in one-dollar bills.^a In 1840 the commissioners of Connecticut complained that several of the banks made discounts upon an understanding that notes were to be put in circulation at a distance. Branch banks in the South employed this method to a considerable degree. In 1817 the legislature of Kentucky gave permission to the Bank of Kentucky and its branches that neither should be obliged to take the notes of the others.^b In Virginia, where the branch system prevailed, the governor in 1846 complained that the banks in Richmond paid out notes of distant branches instead of their own, thus supplying the country with a depreciated currency. In 1857 each bank was required to redeem the notes issued by any other bank in the State.

^a Report of Hazard's Committee, Rhode Island, 1826.

^b Duke, History of the Bank of Kentucky, p. 16.

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5. The use of bank notes as a pledge in borrowing, with the understanding that the notes should not be put into circulation by the creditor bank was another method. This practice was complained of by the bank commissioners of Maine in 1857 and by the commissioners of Massachusetts as late as 1859. One bank would borrow of another on the pledge of its own bills, with the implied understanding that they were to be withheld from circulation during the existence of the loan.

XIV. POST NOTES.

Further evidence in regard to the loose requirements for redemption of notes is to be found in the practice of issuing "post notes." This term is applied to bills payable at some future date, either to "bearer" or to "order," either with or without interest. Originally, as employed by the First United States Bank, they had a legitimate use, being applied to paper used for transmission from one part of the country to another by mail or post, and as they were made payable to order and indorsed at the point of receipt they were rendered safe against loss or robbery. Later, however, this description of notes was superseded by the use of bank drafts or checks, and the term was applied to a kind of paper possessing none of the original attributes except that of being made payable to order. Such notes were issued for the purpose of extending circulation, and as late as 1837 were common in most sections of the country.

Connecticut, in 1815, empowered banks to issue bills up to one-half the paid-up capital, payable in two years after the close of the war.

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In Massachusetts the Suffolk Bank in 1818^a was authorized to make a loan by the issue of "post notes." In 1836 all the banks were permitted to issue such notes up to 50 per cent of the capital in denominations not less than \$5. Interest on such bills was to be paid at 4½ per cent and cease when due. This privilege was used only by weak banks and was repealed within a year.^b

In New York banks occasionally put post notes into circulation, but as a rule only for the purpose of making remittances or in an emergency. In 1830 a law was passed giving the holder of any note which the bank refused to pay on demand an action against the institution for money loaned. Post notes were not declared illegal, but the practical effect of this law was to make them payable on demand. Under the safety fund act, no bank could issue any note unless the same were payable on demand. In 1837 a petition was presented to the legislature that the safety-fund banks be permitted to issue post notes for a limited period;^c a legislative committee, however, reported that this measure would be inexpedient, for banks which had already extended loans would still further increase their obligations. Moreover, the privilege would increase the practice of usury.^d In 1840 the issue of post notes was made a misdemeanor.

In Pennsylvania the Manual Labor Bank of Philadelphia, in 1836, issued post notes in denominations of \$1

^a Whitney, the Suffolk Bank, p. 6.

^b Acts, Mass., 1836, ch. 255, p. 967; Acts, 1837, ch. 224, p. 252; Martin, Boston Stock Market, p. 9.

^c Assembly Document, N. Y., No. 293, April 18, 1837.

^d Assembly Document, N. Y., No. 309, April 25, 1837; see, also, Raguet Currency and Banking, p. 111.

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to \$20. This was a weak bank and soon failed.^a The United States Bank in Philadelphia, in 1837 and 1838, put out sixty-day bills paying 6 per cent interest, and it was estimated that over \$2,000,000 of these notes were held by New York City banks.^b The Second United States Bank at the very outset of its existence voted to issue post notes at sixty days for loans granted.^c

The legislature of Alabama, in 1824, authorized the Bank of the State of Alabama to issue post notes "to order," not exceeding one hundred and twenty days; and in 1834 the Bank of Mobile and its branches were authorized to issue post notes without interest until demand for payment. They were made payable to a specified person for a time not exceeding ninety days. In the following year the bank was allowed to issue only up to one-half of its paid-up capital and one-half of these notes were made payable in specie at Philadelphia, New York, and Boston. An extension of this privilege was granted in 1840 (February 3). Each of the specie paying banks was authorized to issue \$500,000 in post notes.

Mississippi, in 1837, allowed banks to issue post notes to bearer, interest not to exceed 5 per cent and loaned at a rate not exceeding 9 per cent. They were limited in time to from six to thirteen months. The bank was obliged to receive these notes for their own debts and they were made receivable for taxes.^d The Brandon Bank in 1838 made arrangements to redeem its circulation with seventy-

^a Niles, 56:36.

^b Sumner, *History of Banking*, 1:296.

^c January 30, 1817; Sumner, *History of Banking*, 1:79.

^d Acts, Miss., Special Session of 1837.

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day post notes payable in Philadelphia.^a In 1838 the Mississippi Union Bank issued post notes on the ground that there was nothing in the charter which prohibited them, and because of the suspension of specie payments. The governor in the next year complained that this practice forced borrowers to pay at the rate of 22 per cent, and in 1840 the issue of such notes was prohibited.

The Bank of Arkansas issued post notes from its establishment. The Bank of Tennessee in 1839 reported that it had issued post notes on the ground that it was impolitic during suspension to issue paper purporting to be payable on demand without any intention of complying. They had, therefore, issued twelve months' post notes with the promise to redeem them when resumption took place.

Ohio in 1819 prohibited the issue of such notes, but they were in use in 1839.^b In Indiana the court stated that it knew of no principle of common law that required bills or notes to be made payable on demand. As time paper was regarded with disapproval, prohibition was inserted in the banking act of 1829, but this applied only to banks chartered under that act. As banking associations again resorted to such issues in 1838, they were definitely forbidden by the legislature in 1840.

XV. NOTE BROKERAGE.

The establishment of many weak banks after the dissolution of the First United States Bank in 1811, vitiated the currency and led to the issue of notes of depreciated credit. The shaving of bills began to be a regular business,

^a Raguet's Register, 2:43.

^b Report of Bank Commissioners, Ohio, 1840.

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and a general system of brokerage in the buying and selling of notes was developed. Note brokers first appeared in Boston when the State "ran bank mad,"^a and at that time "to the citizens of the Middle States there was nothing more ridiculous than that of discounting bank notes." Such a business naturally flourished during the period of the suspension of specie payments between 1814 and 1817, and by 1818 in every town large or small where there was a bank one or more of these brokers might be found, many of whom made \$20,000 a year profit. Evidence of commercial embarrassment and of losses to bill holders is without limit; countless illustrations can be found in Niles' Register.^b For example, in 1817 it is noted that the bills of the banks of the District of Columbia were from 1 to 1½ per cent below par in Baltimore, only 40 miles away, and the bills of the Baltimore banks suffered about the same depreciation in Washington. The bills of the State Bank in North Carolina were 4 per cent below par in Baltimore, while those of the latter place were at the same discount in North Carolina. "Since I began to write this article I have paid as much discount on bank notes to get Baltimore paper as my semiweekly marketing costs me."^c Not one trader in a hundred dared to demand of a bank the payment of \$1,000 of its notes. The bank regarded every man as an enemy that asked it to meet its own obligations. Niles recalls that he was among the most

^a Niles, 15:218, November 21, 1818.

^b For prices of bank notes 1814-1841, see Gouge, *Journal of Banking*, pp. 354-355.

^c Niles, 12:262, June 21, 1817.

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zealous to support the banks in their refusal to redeem during the war period, but now in times of peace, when "I see speculators and stock jobbers and money changers fatted like stall-fed oxen by a sequence of things that is against all law and justice by the patriotism of the people, it cuts me to the quick that I still suffer at the rate of \$300 or \$400 per annum of my hard-gained earnings in discounts on bank paper received at par, and as good, if not better, as that which they have been pleased to fix upon as a standard of value."^a In 1820, when conditions had improved, the paper of Boston banks could not be converted into passable money at Baltimore for less than 1 per cent and the discount on Baltimore bank bills was even greater at Boston. Niles contrasts this with the period eight or nine years before, when almost every bank note received by him from any part of the United States served all the purposes of specie without the aid of a broker and without loss.^b At one time a large part of the current money in Baltimore was composed of notes of banks in the District of Columbia and Virginia, and was at a discount of from 1 to 1½ per cent. The banks consequently agreed to accept these notes at what was called "short entries," to be carried out at the end of forty-five days, equal to a discount of from three-fourths to 1 per cent.^c In 1828 it was estimated that the cost for brokerage to citizens of Baltimore amounted to \$45,000 a year. Banks also engaged in this brokerage; in

^a Niles, 12; 262, June 21, 1817.

^b *Ibid.*, 19:81, October 7, 1820; for tables of prices of bank bills, see *Ibid.*, October 8, 1818, 14:396, 415; July 10, 1819; 16:321, 38:197 contains a table showing prices between 1816 and 1829.

^c *Ibid.*, 24:257.

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1823 it was reported that two Connecticut banks placed in the hands of New York brokers a large sum for the purpose of purchasing notes of other Connecticut banks which were below par and then collecting on these banks. A profit of 15 per cent per annum was thus made.^a

As late as 1834 the bills of New England banks were at 2 per cent discount in Baltimore, and those of New York State outside of New York City were from 2½ to 3 per cent. Virginia money was from 4 to 5 per cent discount in Baltimore, good banks in Ohio at 10 per cent, and in Boston the notes of New York City were at 1 per cent discount, and those of Philadelphia and Baltimore at 2 per cent.^b Niles relates the following incident as an illustration of the embarrassment of using local bank currency in that year: A gentleman of Connecticut called at his office in Baltimore to pay \$5; he offered a \$20 bill of the Phoenix Bank of Hartford, and received a \$5 Philadelphia note and one of \$10 of the Bank of the Valley of Virginia, with the remark that the latter was better in Baltimore than his own, the Hartford bill. The \$20 note received by Niles was sold at 1½ per cent discount, or at a loss of 30 cents on the \$5 received. The gentleman carried the Valley note home to Connecticut, but could not dispose of it at less than 8 per cent discount, and consequently returned it. Niles thereupon sent him a bill on a Hartford bank directly obtained in exchange for the note which he had transmitted with 7½ cents in his favor for such exchange at the brokers' rates, which he waived.^c According to Niles, the dis-

^a Niles, November 22, 1823.

^b *Ibid.*, 46:17, 85, 132, 133, 190, 191.

^c *Ibid.*, 47:218.

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count paid by New York merchants on Western bank notes was over \$500,000 per annum.

Another illustration is furnished by Lowndes, in his *Letters to Calhoun*,^a in a condensed journal of a traveler who, about 1840, left Virginia for the West.

"Started from Virginia with Virginia money; reached the Ohio River; exchanged \$20 Virginia note for shinplasters and a \$3 note of the Bank of West Union; paid away the \$3 note for a breakfast; reached Tennessee; received a \$100 Tennessee note; went back to Kentucky; forced there to exchange the Tennessee note for \$88 of Kentucky money; started home with the Kentucky money. In Virginia and Maryland compelled, in order to get along, to deposit five times the amount due, and several times detained to be shaved at an enormous per cent. At Maysville wanted Virginia money; couldn't get it. At Wheeling exchanged \$5 note, Kentucky money, for notes of the Northwestern Bank of Virginia; reached Fredericktown; there neither Virginia nor Kentucky money current; paid a \$5 Wheeling note for breakfast and dinner; received in change two \$1 notes of some Pennsylvania bank, \$1 Baltimore and Ohio Railroad, and balance in Good Intent shinplasters; 100 yards from the tavern door all notes refused except the Baltimore and Ohio Railroad; reached Harpers Ferry; notes of Northwestern Bank in worse repute there than in Maryland; deposited \$10 in hands of agent; in this way reached Winchester; detained there two days in getting shaved. Kentucky money at 12 per cent, and Northwestern Bank at 10."

^a Pp. 60-61.

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Efforts were made in some States to restrict this traffic, as, for example, in Maryland, where a law was passed in 1818 forbidding officers of banks in particular, as well as other persons, from buying or selling the notes of any bank in the State for less than the nominal value of the notes, under penalty of a forfeiture of double the sum.^a This, however, did not restrain dealings in notes of foreign banks, and in 1840 it was reported that some of the banks purchased such notes at a discount.^b

XVI. SYSTEM OF VOTING.

In order to encourage participation in bank ownership by persons of small means, and as a further check against the monopoly of power by the rich, a system of regressive voting for many years was almost universally followed. Even Hamilton criticised the charter of the Bank of North America because it adopted the principle of one share, one vote, which promoted monopolization of the power and benefits of the bank. The articles of association of the Bank of New York, 1784, in which Hamilton was interested, limited the number of votes which a stockholder could have: one vote for every share up to 4; for 6 shares, 5 votes; for 8 shares, 6 votes; for 10 shares, 7 votes, and for every 5 shares above 10, 1 vote.^c

The First United States Bank allowed 1 vote to 1 share, 2 votes to 3 shares, 3 votes to 5 shares, and so on until 100 shares had 20 votes. Different scales were adopted in different States. In the Providence Bank in Rhode

^a Acts, Maryland, session 1818, ch. 191.

^b Report of Bank Commissioners, Maryland, 1840.

^c Domett, Bank of New York, p. 12.

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Island, 1791, 100 shares gave 20 votes, and 200 shares 30 votes, the maximum allowed to anyone;^a in the Exchange Bank of Providence, 1801, the upper limit was extended to 100 shares; in 1804, in the charter of the Rhode Island Union Bank, the restriction, however, was abandoned and for the first time in that State voting power was proportionate to shares held.^b Connecticut likewise rejected this system in 1796, and made voting power proportionate to share interest. In Massachusetts there was 1 vote for 1 share, and for every 2 shares above 1, 1 vote with a maximum number of 10. Later the rule was 1 vote for 1 share and 1 for every 10 additional shares, until 10 votes, the maximum, was reached. By an act of 1840, no one by proxies could cast more than 50 votes, and no officer of the bank more than 10.^c In New Hampshire, voting at an early date was according to stock.^d New York also adopted the principle of restricted voting.^e In New Jersey, down to 1833, the charter restricted the number of votes, and occasionally after that date.

In Pennsylvania the system of graded voting was continued in the general act of March 25, 1824, and also incorporated in the charter given to the Bank of the United States in 1836. Maryland introduced the graded system at an early date, and in 1820, a more curious restric-

^a Stokes, *Chartered Banking in Rhode Island*, p. 4.

^b *Ibid.*, p. 17.

^c Acts, 1840, ch. 61, p. 208.

^d Commercial Bank, Portsmouth, 1825.

^e Mechanics' Bank, 1810, 1 vote for every share up to 20; 1 for 5 shares above 20 up to 100; 1 vote for every 10 above 100; Bank of America, 1812, maximum number, 30 votes.

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tion was approved, whereby stockholders living within 10 miles of a bank could not vote by proxy, except females and persons unable to attend by reason of bodily sickness. Virginia continued the principle of a decreasing scale in her general law of 1837.^a

Alabama, in the charter of the Planters' and Mechanics' Bank, 1816, set 100 votes as the limit.^b Florida, in 1829, also imposed a limitation of voting upon the stockholders of the Bank of Florida, and in the charter of the Bank of Pensacola, 1831, restricted the maximum to 30. Before the bank went into operation, however, the charter was amended so as to give proportional rights. By a charter in 1833, 1 vote to a share was repeated, but the maximum number of votes was fixed at 100. In the Commercial Bank of New Orleans, 1833, no one could have more than 100 votes, and only those living more than 5 miles from the city could vote by proxy. It was also generally required that shares should be held for at least three months in order to entitle the holder to vote.

Ohio, in the charter of the Bank of Marietta, 1808, the first established, made votes proportional to shares, but in 1809 adopted a regressive scale.^c The ratio, as adopted in the charter of the Franklin Bank in 1833, was 1 vote for each share up to 20; 1 vote for 5 shares above that, with a maximum of 50. The Louisville Bank, in Kentucky, 1833, gave 1 vote for every share up to 50; for every 5 above 50, 1 vote; and for every 20 above 100,

^a Laws, Va., 1836-37, ch. 82, sec. 6.

^b Toulmin's Digest, p. 39.

^c Bank of Steubenville.

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1 vote. The charter of the State Bank of Indiana, 1834, limited the maximum number of votes to 100;^a later, in a charter of 1855, the rule was 1 vote for each share up to 50; 1 vote for every 5 shares from 50 to 100; and 1 for every 10 shares over 100.^b Missouri, in 1813, fixed a scale making 17 votes as the maximum.

XVII. LIABILITY OF DIRECTORS.

In the early development of banking, great stress was laid upon faithful service by directors, and in order to secure this, heavy liabilities were placed upon them. As a rule, the members of the managing board were made individually liable in their private capacities if debts or liabilities exceeded the legal limit. Directors could exonerate themselves if they were absent, or if they dissented when the excess of indebtedness was contracted, by giving immediate notice to that effect. Such was the case in the charter of the Massachusetts Bank, 1784, and of the First Bank of the United States, 1791. The rule established for this bank was almost universally copied in the subsequent charters of local institutions.^c Frequently notice of dissent had to be given to some public official as well as to the stockholders, as, for example, in the case of the First United States Bank, to the President of the United States, and to the mayor of the city by the charter of the Bank of Alexandria, 1792, and in Maryland, to the governor.

^a Laws, Ind., 1834, ch. 7, sec. 3.

^b Ibid., 1855, ch. 111, sec. 27.

^c General law of Pennsylvania, 1824; general law of Massachusetts, 1829; branch of the Bank of the State of Alabama, Mobile, 1832; Franklin Bank, Cincinnati, 1833; Louisville Bank, 1833; Farmers' and Mechanics' Bank, Hartford, 1832.

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In Vermont and Connecticut liability for redemption of note issues was imposed upon the management. In Vermont "directors were made liable for the debts of their bank should successive issues take place under their administration. Each director, too, was obliged to give a satisfactory bond, usually \$8,000, as a guarantee of the faithful performance of his duties. In Connecticut the directors and cashiers were held liable as joint and several debtors should the debts of the institution exceed the amount specified in the charter."^a

In some charters, directors were made liable if the capital of the bank was impaired by the payment of a dividend. Maryland recognized this principle in 1804, in the charter of the Union Bank in Baltimore; Missouri, in 1813, in the charter of the Bank of St. Louis; and Virginia adopted it in her general law of 1837; while Congress imposed this obligation upon banks incorporated in the District of Columbia in 1817. Rhode Island, after the scandal attached to the failure of the Exchange Bank in 1805, made the directors personally liable for all debts of the bank after the property of the corporation was exhausted.^b Directors and officers in the Arcade Bank, Rhode Island, 1833, who committed fraud or embezzlement forfeited their shares, in addition to liability for prosecution. Impairment of capital, irrespective of the cause, made directors personally liable in the general banking law of Pennsylvania, in 1824, and the same was true of the Franklin Bank, Cincinnati, 1833, and the

^a L. Carroll Root, *Sound Currency*, 8:216.

^b Stokes, *Chartered Banking in Rhode Island*, p. 21.

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Louisville Bank, 1833. In New Jersey, beginning with 1812, directors were liable for impairment of capital paid out as dividends as well as for incurring indebtedness in excess of legal limit.^a By a charter, in 1818, directors were liable for all notes for which the bank refused redemption;^b and this was repeated in charters of 1828, 1830, and 1855.

North Carolina, in the charter of the Mechanics' Bank, Newburne, 1833, made the illegal extension of the bank's credit a felony on the part of the directors, and in another charter, in 1846, defined it as a misdemeanor. The charter of the State Bank of Indiana made directors liable for excess of debt and also in case of fraudulent insolvency.^c

XVIII. LIABILITY OF STOCKHOLDERS.

In the first bank charters no special liability was placed upon stockholders, and attempts to introduce this principle did not generally meet with success. Pennsylvania, in 1808, passed a law imposing individual liability, but repealed it two years later.^d Finally, in 1811, the legislature of Massachusetts, owing to an increasing distrust of banks, made stockholders individually liable to the amount of shares held, if any loss arose on account of mismanagement, as a condition for securing further extensions of charters. An example of the loose liability then existing is seen in the action of the Hallowell-Augusta Bank, in Maine, which, in 1813,

^a Laws of New Jersey, 36 Assembly, 2 sess., pp. 11, 12, sec. 24.

^b Sussex Bank, Priv. Acts, N. J., 42 Assembly, 1 sess., p. 61.

^c Laws, Ind., 1834, ch. 7, secs. 98, 101.

^d Laws, Penna., 1807-1808, p. 186.

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divided 75 per cent of its capital among stockholders, although there was outstanding a large amount of bills. The supreme court of Massachusetts, in 1819,^a decided that the individual stockholder was not liable to a holder of notes.^b In 1849 liability was extended to cover redemption, whether failure was due to maladministration or not. In New Hampshire, by the charter of the Concord bank, 1806, stockholders were made jointly and severally liable for the redemption of bills issued; this requirement was, however, dropped in the renewal of the charter in 1824,^c but as a rule unlimited liability prevailed. In Rhode Island, stockholders' liability beyond the amount of investment was not introduced until 1814, in the charter of the Union Bank, and then only when the directors violated the bank process act;^d but beginning with 1833 nearly all charters provided for unlimited personal liability of stockholders.^e This discouraged the investment of trust funds in bank stock, as well as ownership by silent partners who did not care to concern themselves actively in the affairs of their institutions.^f In Vermont a bank was chartered in 1817, which made stockholders liable in their personal fortunes, but owing to the risk thus incurred it was not put into operation. In the following year this burden was removed, and as a rule liability was imposed upon the management rather than upon the stockholders.

^a *Speare v. Grant*, Massachusetts Reports, 16, p. 19.

^b *Gray v. Portland Bank*, Massachusetts Reports, 3, pp. 378-383.

^c Report of Bank Commissioners, New Hampshire, 1840.

^d Stokes, *Chartered Banking in Rhode Island*, p. 30.

^e *Ibid.*, 40.

^f W. Phillips, *Political Economy*, p. 263.

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In New York, when the safety fund system was under discussion in 1829, it was argued that protection of a bank's creditors could be accomplished better by an insurance fund than by placing the liability upon stockholders and directors; the latter would not invest capital subject to extended liability so long as it was possible for speculators to get control and mismanage the bank.^a As a result, stockholders in the safety fund banks enjoyed freedom of liability, and nonliability was extended to stockholders of the free banks authorized in 1838, but in the State constitution of 1846 stockholders of all banks were made responsible for an amount equal to stock paid in. In Maryland, the constitution of 1851 required double liability.

Stockholders in the Bank of Alexandria (Va.), 1792, were liable in proportion to their holdings in case debts exceeded four times the capital, but only when the directors' property was not sufficient.^b In charters granted in the middle of the century the liability covered the circulation and express contract debts of the banks.^c Florida, in 1829, provided for liability in proportion to shares, and in 1843, made the stockholders of the Bank of Florida liable for three times their stock. Two years later the constitution made stockholders individually liable for all debts in case of dissolution or suspension of redemption.

^a See Plan of Joshua Forman; Message of Governor Van Buren, January 26, 1829.

^b Laws, Va., 1792, ch. 76, sec. 13.

^c Laws, Va., 1850-51, ch. 58, sec. 10; Laws, 1855-56, ch. 80, sec. 21.

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In Ohio a legislative committee, in 1839, reported in favor of individual liability of stockholders to be applied when banks owed one and one-half capital or when any bank, from insolvency or suspension of more than thirty days, was subject to the forfeiture of charter, and in 1842 individual liability was imposed. The state treasurer of Michigan, in 1850, stated that the principle of individual liability of stockholders, which had been previously enacted, while it exercised a restraining influence, was of small value to the noteholder in case of failure. Collection by the tedious process of the law forced the holder of notes to sell them at the highest price in the market. The Indiana stockholders in the state bank were made liable in case of fraudulent insolvency for debts which could not be collected from directors.^a Double liability only was adopted in the general law of 1855.^b The charter of the Shawneetown Bank, in Illinois, provided that the private property of stockholders should be held for redemption of bills. By the banking law of Wisconsin, 1855, stockholders were required to execute a bond to the amount of one-fourth of the circulating notes, as a security over and above that deposited to indemnify the bill holder.

XIX. QUALIFICATIONS OF DIRECTORS.

Further evidence of the early fear of a money power is found in the restrictions placed upon the selection of directors. These limitations were of a varied character, including conditions as to length of service, residence,

^a Laws, Ind., 1834, ch. 7, sec. 102.

^b Laws, Ind., 1855, ch. 7, sec. 22.

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incapacity to serve as director in more than one bank, ineligibility of public officials, and occupation. Later, ownership of a certain amount of stock was sometimes imposed.

(a) *Length of service.*—Hamilton, in his bank report of 1791, objected to the charter of the Bank of North America, because it did not provide for the principle of rotation in the board of directors, so as to lessen the danger of combinations among directors to use the bank for personal purposes or to monopolize its funds for the accommodation of any particular set of men. In accordance with this view, the charter of the First United States Bank, 1791, provided that not more than three-fourths of the directors, exclusive of the president, should be eligible for the next succeeding year. This proportion is to be found in many charters of state banks. Massachusetts followed it in her early acts,^a and Connecticut adopted this rule in the charter of the Hartford Bank, 1792. Maryland, in the act incorporating the Bank of Baltimore, 1795, made the proportion two-thirds, but in 1800 this restriction was repealed, subject to the consent of the stockholders. For many years, however, no advantage was taken of this privilege. By the charter of the Union Bank of Maryland, 1805, no director could serve for more than three years until two years had elapsed. In the charter of the Second United States Bank, 1816, no director could hold office more than three years out of four in succession. By this time, however, such a restriction was being dropped in many

^a Union Bank, 1792; Nantucket Bank, 1794; Newburyport Bank, 1795.

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States, and Cheves, president of the bank in 1821, complained that its application deprived his institution of the services of qualified men, and as it was no longer to be found in charters of other respectable banking institutions, it ought not to be imposed hereafter on the Bank of the United States.^a Cheves was hardly justified in this sweeping statement, for the restriction was incorporated in the general banking legislation of Pennsylvania, 1824, and also in the charter of the Bank of the United States, granted by that State in 1836. The charter of the Louisville Bank of Kentucky, 1833, limited eligibility to two years in succession.

(b) *Residence*.—A common restriction was the requirement that directors should be residents of the State in which the bank was organized, but in many cases a more definite residence was prescribed. By the general banking law of Massachusetts, 1829, a majority of the directors of its banks must be residents of the county in which the bank was situated, and in 1853 this requirement was repeated with a modification of residence to within 10 miles of the bank. The charter of the Washington Bank in Rhode Island, 1800, which was organized for the special benefit of farmers and mechanics, required that two-thirds of the directors and the president should be residents of the county.^b A legislative committee in 1836 noted with approval that the directors of a large majority of the banks resided in or near the town where the bank was established, but reported that there was

^a Memorial to the House of Representatives, January 21, 1821, Finance, 3:587.

^b Stokes, *Chartered Banking in Rhode Island*, p. 13.

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one exception—a bank in Foster, six of whose thirteen directors resided in Providence.

In New Jersey restrictions as to residence were not uniform. In a charter of 1822, a director must be resident of the county in which the bank was located; in the Peoples' Bank at Paterson, 1824, seven out of the thirteen directors must be inhabitants of Paterson; in another charter in the same year, they were required to be inhabitants of the county; in yet another, they need simply be citizens of the United States; and in a fourth, citizens of New Jersey. In a charter of 1828 the president must reside within 3 miles of the bank, but later the distance was increased to 10 miles. In a charter of 1834 eight of the thirteen directors must reside in the town where the bank was established. In 1835 a charter was granted permitting two directors to be citizens of Pennsylvania, and by another in 1855 eight out of thirteen directors must reside in Newark.

All of the thirteen directors of the Girard Bank in Philadelphia were required to be residents either of the city or county of Philadelphia. The charter of the Mechanics' Bank in Baltimore, 1806, required the directors to be residents of that city, but this restriction was removed in 1815, so as to permit the service of residents of any part of the State.^a The charter of the Exchange Bank of Virginia, 1837, permitted two directors to be residents of North Carolina.^b In 1838 the governor of Louisiana vetoed a bill which provided that a director should have

^a Laws, Md., 1814, ch. 53.

^b Laws, Va., 1836, ch. 83, sec. 17.

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five years' residence instead of one. In Missouri the charter of the Bank of St. Louis, 1813, demanded that all of the directors should be residents either of St. Louis or of Ste. Genevieve.

(c) *Incapacity to serve as director of more than one bank.*—This restriction was common to all. In 1811, Massachusetts, in a charter of the State Bank, forbade any director to serve in the same capacity in any other banking institution, and this requirement was later incorporated in the Revised Statutes, and also in the safety-fund act of New York in 1829. The same limitation is to be found in the general banking law of Pennsylvania, 1824. As a rule, this prohibition was extended so as to exclude those who were partners in trade with a director in any other bank.

(d) *Ineligibility of public officials.*—By a general law of Pennsylvania, 1824, all executive and judicial officers and members of the legislature were declared ineligible. This restriction, although dropped in some of the subsequent charters, reappeared in that of the Bank of the United States in 1836. By the charter of the Farmers' Bank of Virginia, 1812, officials of both the State and the United States were declared ineligible,^a and this restriction was continued in the general law of 1837; in 1842, general agents of manufacturing and mining companies were also declared ineligible. In the charter of the Bank of Florida, 1828, and again in 1845, government officials were excluded. Certain state executive officers were

^a Acts, Va., 1812, pt. 1, vii, sec. 15.

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also excluded from the directorates of the State Bank of Indiana.

(e) *Ownership of stock*.—As a rule, a director was required to be a stockholder, but not necessarily a large owner; in Massachusetts a single share qualified. By the charter of the Exchange Bank in Providence, R. I., 1801, he must own 20 shares, and this amount was repeated in subsequent charters. In 1831, in the charter of the Bank of America in New York, an amendment was inserted requiring directors to own \$1,000 of stock. There was, however, no general rule in that State; in some banks with a capital not over \$100,000 a director must own \$1,000, while in one with a capital of \$250,000 only \$250 was required.^a In the Merchants' and Mechanics' Bank of Virginia, 1834, a director must own 10 shares, and by a general law of 1837, 5 shares were fixed as the rule. Ten shares were imposed in the charter of the Union Bank at Tallahassee, Fla., in 1833; and in that of the Union Bank of Louisiana, 1832, 50 shares. In the case of the Franklin Bank of Cincinnati, 1833, 10 shares were required; in the Bank of Kentucky, in the same year, 25 shares; and in the State Bank of Indiana, 1834, 5 shares. A more exceptional qualification was a requirement that a certain number of directors should be engaged in some particular occupation. For the management of the Mechanics' Bank of New York, 1810, seven of the thirteen directors were required to be members of the General Society of Mechanics and Tradesmen of the city of New York, of which four must actually be following a mechan-

^a Report of Bank Commissioners, New York, 1835.

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ical profession. In the general banking act of Pennsylvania in 1824, provision was made for the Mechanics' Bank in Philadelphia, in which no person was eligible for director unless he was a mechanic actually engaged in some mechanical occupation which he had followed for one year; and in the Farmers' and Mechanic's Bank at Pittsburg the directors must be mechanics or farmers.

The charter of the Mechanics' Bank in Baltimore, 1806, demanded that nine of the fifteen directors should be "practical mechanics or manufacturers." In 1810 this requirement was defined by a special act so as to mean those who "shall have actually learned and wrought at some mechanical or manufacturing trade for a term of three years," and shall have been so engaged for at least one year next preceding election.^a In 1818 this restriction was further modified so as to require only a majority of the directors to be so engaged.^b In Ohio, the charter of the Farmers' and Mechanics' Bank of Cincinnati, 1813, required that one-third of the thirteen directors should be practical farmers, and one-third practical mechanics.^c

XX. REPORTS FROM BANKS; SUPERVISION.

Legislatures were slow in requiring reports or annual returns from banks in regard to their condition. Indeed, during the first part of the century, the accounts of banks were guarded with secrecy; and writers on banking problems frequently refer to the lack of data. Matthew Carey, for example, writing in 1811 on the First Bank of the United

^a Laws, Md., session, 1810, ch. 134.

^b Laws, Md., session, 1817, ch. 39.

^c Drake, Pictures of Cincinnati in 1815, p. 15.

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States, complained that he "labored under a most distressing destitution of material and documents."^a This bank by its charter was required to make regular returns to the Treasury Department, but only two of these found the light of publication. "A Friendly Monitor," writing in 1819, refers to his "embarrassment" in obtaining the most simple information in regard to the bank (Second Bank): "If I ask a director, the seal of his finger is significantly on his lips." Dr. Eric Bollman, in his essays, also alludes to this difficulty.^b When Niles began to devote a considerable amount of attention to the banking question between the years 1818-19, his efforts to collect information were in a large measure unsuccessful. Secretary Crawford, in his report in 1820, was unable to obtain reliable data as to the capitalization of banks, and Gallatin, who wrote at length on the subject of banking in the United States, in 1831, obtained different figures from those of Crawford, both as to capital and circulation; for example, Crawford gave the circulation in 1815 as \$110,000,000, while Gallatin put it at \$45,000,000. Gouge, writing in 1833, says that for seven years he had been collecting accounts of banks, but did not think it worth while to publish them. He had a list of 28 failed banks which Gallatin had not listed, and he notes that the latter had to guess at the amounts of specie held by many banks.

In the first charter granted by Massachusetts, that of the Massachusetts Bank, 1784, it was provided that any one appointed by the legislature should have access to the

^a Letters to Dr. Adam Seybert, 1811, p. v; see also Tucker, *Money and Banks*, p. 210.

^b See also Dunbar, *Accounts of First United States Bank*, in *Economic Essays*, p. 171.

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bank.^a This right was repeated in subsequent charters. In 1802 the legislature requested the governor to lay before it at the next session the most recent bank statements.^b This was followed in 1803 by an act calling for semiannual statements to be made to the governor covering the following items: Capital paid in, debts due the bank, deposits, notes in circulation, coin and metals on hand, notes of other banks, distinguishing between those of Massachusetts banks and those outside; this statement was to be signed by a majority of the directors and attested by the cashier.^c In 1806 the cashier was required to take oath and the range of items was slightly amplified, so as to include the value of real estate. A distinction was also made between "debts on interest" and "debts not on interest." In the circulation, the amount of notes under \$5 was called for and also the amount on hand.^d In 1807 the banks were obliged to state the last dividend paid and their profits at the time the dividend was declared. In 1813 a further step was taken by adding a penalty of \$5,000 for neglect on the part of the bank to make the return within fifteen days.^e In 1838 a board of three bank commissioners was established, appointed by the governor, who should make annual examination of all the banks in the Commonwealth, with special reports if requested by the governor. If the condition of any bank was hazardous to the public or to those having funds in its custody, or if it had exceeded its powers or had violated the banking laws, the commissioners were authorized to pro-

^a Laws, 1780-1800, 1:115.

^b Resolves, 1802, p. 380.

^c Acts, 1802, ch. 132.

^d Acts, 1805, ch. 111.

^e Acts, 1813, ch. 140.

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cure an injunction from the supreme judicial court. This board continued in existence for five years, during which time it procured injunctions against seven banks. In 1851 the board of bank commissioners was reestablished, with practically the same powers and duties as the former board.

Connecticut, in 1803, enacted that the State should be furnished by the five banks which held the public deposits with certain data in regard to their condition, not oftener than once a month; this was not for the protection of depositors, but for the benefit of the State.^a In 1822 a general act was passed requiring the incorporated banks of the State to report to the comptroller certain statements covering the capital stock, debts due, deposits, notes in circulation, etc., but there was no uniformity in rendering the returns. No provision was made for official inspection or for the publication of reports. According to Woodward, the historian of the Hartford Bank, "as the banks had pursued a conservative course, and as no machinery was supplied for correction of abuses, the law took but a slight step forward in the way of supervision. Perhaps the legislature wished to emphasize the right of the people to know the condition of the institutions which furnished their currency and had custody of their notes."^b In 1836 the state treasurer, comptroller, and commissioner of the school fund were appointed a committee to examine banks, with authority to inspect all books and papers and to examine bank officials under oath. When the Hartford

^a Woodward, *The Hartford Bank*, p. 83.

^b *Ibid.*, p. 127.

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Bank was called upon for a total statement of assets and liabilities its directors maintained that the proposed method of inquiring into its affairs encroached upon the privileges of its charter. The bank also claimed that its charter was irrevocable and not subject to amendment without consent of its stockholders, but in order to avoid suspicion, it granted a full examination, reserving, however, its rights. In 1837 a law was passed providing for the annual appointment by the legislature of two bank commissioners whose salaries were to be paid by the banks according to their capitalization. The Hartford Bank and two others refused to pay their assessment, but in 1841 the former settled the proportion levied upon it without acknowledging any legal liability, but as an act of grace, believing "that the services of judicious bank commissioners are highly beneficial to the public interest."^a From this time on opposition to supervision gradually disappeared.^b

In Vermont a board of three bank commissioners was authorized in 1831. In New Hampshire it was reported in 1840 that no examination of the Concord Bank had been made since 1812. In Rhode Island annual returns were required, but it was asserted that these did not furnish a satisfactory disclosure of the condition of banks. Banks set their affairs in order that they might make a favorable showing. In 1836 a board of bank commissioners was established; in 1842 the act was repealed and semiannual returns only were provided for; later, in

^a Woodward, *The Hartford Bank*, p. 141.

^b See also *Merchants' Magazine*, 39:97.

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1849, the returns were made annual, and again in 1856, a board of commissioners was revived.

Down to 1824 banks in New York were not required to make returns regularly. In 1827, by a general law, reports to the state comptroller were demanded, and two years later the safety-fund act provided for three bank commissioners, one appointed by the governor and two by the banks, with power to make quarterly visits. Banks were also required to report annually to the commissioners. In 1835 reference was made to the beneficial effects of periodical examinations, and the existing system was contrasted with former conditions when a bank director deemed it one of his most important duties to throw an impenetrable veil of secrecy around all the proceedings of his institution. It was expected that the country banks would be represented by one commissioner and the city banks by another, and that these would be a check upon each other. The governor and senate appointed one, the banks in the southern part of the State another, and the remaining banks a third. In 1837 the law was changed so as to give the appointment of all three to the government; but this brought them "within the vortex of the great political whirlpool of the State."^a In 1843 the board of bank commissioners was abolished and returns were made to the comptroller. In 1853 all banks, banking associations, and individual bankers in New York city were required to publish a weekly average statement of their condition.

In New Jersey annual reports to the legislature were required, beginning with 1812, but the number of items

^a Report of Comptroller of New York, 1848.

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was small. In an act of incorporation in 1824 failure to report for three years forfeited the charter.^a In 1837 the returns were made more detailed, including capital, stock notes, stock securities for loans, specie, real estate, debts classified, surplus, expenses, dividends, amount of discounts, interest, and deposits.^b In 1850 failure to file a report entitled the chancellor to begin proceedings to dissolve the bank.^c

The Bank of Pennsylvania in 1803 by its charter was required to make a report annually to the legislature. The act of 1814, creating a large number of new banks, demanded that annual reports be made to the auditor-general, but complaints were subsequently made that down to 1833 the Bank of Pennsylvania and Bank of North America did not make regular returns.^d

In Maryland, the charter of the Bank of Baltimore, 1795, provided for annual reports, or oftener, if required, and gave power to the treasurer of the State to inspect the general accounts of the bank, but not the accounts of any private individual. This examination was not to be used for any other purpose than for forming a just opinion of the state of the bank relative to public safety and the profits of the bank. (Art. 19.) A similar provision is to be found in the charter of the Mechanics' Bank of Baltimore, 1806.^e This requisition of an annual report or the

^a Priv. Acts, N. J., 39 Ass., p. 41, sec., 14.

^b Acts, N. J., 62 Ass., pp. 11-12, sec. 2.

^c Acts, N. J., 74 Leg., pp. 151-152, sec. 30-31.

^d Gouge, *Journal of Banking*, 1:405; according to Sumner, *History of Banking*, 1:175, banks in Pennsylvania made no regular returns to the legislature until after 1817.

^e Bryan, *History of State Banking in Maryland*, pp. 33-35.

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right of inspection was generally incorporated in Maryland charters, but as the State did not endeavor to enforce its powers the banks paid little attention to it. Repeated acts requiring the statements to be made availed little until 1826, when a penalty was imposed for noncompliance.^a

Virginia, in the charter of the Bank of Alexandria, 1792, called for an annual report to be presented to the governor "truly stating the situation of the bank and its notes,"^b and the charter of the Bank of Northwest Virginia, 1817, demanded reports on four quarterly dates. In 1831 the legislature required a statement as to the amount of debts outstanding on loans made during the preceding year, classifying them into good, bad, and doubtful.^c In 1834 the charter of the Merchants' and Mechanics' Bank called for the amount paid in, real estate, debts due and from the bank, gold and silver deposits, bills in circulation and bills of other banks, dividends and surplus.^d In 1837 the directors were required to make an examination once in three months and to enter their results on the records of the bank. The directors were also required to transmit to the governor quarterly statements of the condition of the bank, including the items above named and also dealings in exchange and premiums paid on them, amounts of bad and doubtful debts with the classification of notes according to denomination, and bills in circula-

^a Bryan, *History of State Banking in Maryland*, pp. 34-35, 70.

^b Laws, Va., 1792, ch. 76, sec. 14.

^c Bank of Virginia and Farmers' Bank of Virginia; see Resolves, 1830-31, No. 4.

^d Laws, Va., 1833-34, ch. 72, sec. 12.

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tion.^a The statement was to be open to the stockholders at their regular meeting, or to any three owning 100 shares thirty days before election; and the legislature was given the right of inspection. In 1856 the Bank of Virginia was required, in addition to the statutory report, to include the debt due by banks, debt due to banks, discount of inland and foreign bills, loans to directors, specie, circulation, and deposits.^b

In North Carolina charters generally required the making of an annual report; the statement, however, was of simple character, being a condensed summary of the bank's resources and liabilities. Examinations were sometimes made by special legislative committees. The constitution of Florida, 1845, required quarterly reports to be made to the governor and also that banks be open to inspection at any time by an examiner appointed by the governor. The branch of the Bank of the State of Alabama, 1832, was required to make reports to the general assembly, and the legislature had the right to inspect the general accounts. In 1837 a dispute arose in Louisiana as to whether a legislative committee could inquire into the proceedings of the Bank of Orleans. The bank refused on the ground that this was not demanded in the original charter in 1811, nor in the renewal in 1823, nor in the amendments made in 1831. The bank, however, was willing to permit inspection provided it was not regarded as a visitorial power or claimed as a right, and justified its position because the State had in the charters of some

^a Laws, Va., 1836-37, ch. 82, sec. 6.

^b Laws, Va., 1855-56, ch. 60, sec. 6.

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other banks expressly retained the power of inspection. On the other hand, it was maintained that as the State was the guardian of the currency, it had this right in order to protect the public against depreciation.

In Ohio, a law was passed, February 23, 1816, providing that semiannual statements be made to the auditor of the State. Very few banks complied, and the committee of the legislature in 1820 reported that there were twenty-three delinquents, some of whom had let a whole year intervene between reports, some had made returns without oath or affirmation of the cashier, and others had made no returns since they went into operation. Only one bank had strictly obeyed the law.^a Other evidence of the inaccuracy of reports is to be found in the report of a legislative committee in 1819, where it is stated that some of the banks in their returns had omitted their real estate; some their accounts with other banks, simply stating in general terms that the balances were in their favor, while others omitted to state the number of shares owned by the State or the amount of surplus and undrawn dividends remaining in the bank. In 1839, provision was made for a board of three bank commissioners. By the charter of the State Bank of Indiana, in 1817, the governor and the general assembly could call for statements not oftener than once a month, which should include the amount of capital, debts due, deposits, notes in circulation, and cash on hand.^b

^a Senate Journal, Ohio, 1820, p. 175.

^b Laws, Ind., 1817, ch. 41, sec. 10; see also Laws, 1834, ch. 7, secs. 65, 66; Laws, 1842, ch. 70; Laws, 1855, ch. 7, sec. 27.

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The returns which were made by banks were in many cases incomplete and full of ambiguities. The term "cash," for example, was not accurately defined. In the case of country bank notes it sometimes included city bank notes.^a Bank commissioners in Connecticut, in 1842, thought that the reports then made in that State were useless, and if continued should be more minutely classified. In New York, in the same year, it was complained that for several weeks prior to a return banks commonly made a forced preparation.^b

XXI. BRANCHES.

The question of the utility of extending the operations of a bank by the organization of branches was raised at an early date. Hamilton, in his report on establishing a national bank, briefly refers to the subject; he admitted that branches might afford more general accommodation and would lessen the danger of a run upon the bank, but on the other hand, the complexity of such a system would be apt to inspire doubts which ought to be avoided in the introduction of a general banking system. Each branch, also, must be under a distinct, though subordinate direction, to whom a considerable latitude of discretion must be entrusted. As the property of a whole institution would be liable for the engagements of each part, the credit of the parent bank would depend upon the prudence of the directors of each branch. In addition, it might be noted that while a bank could through branches collec-

^a See Gouge, *Journal of Banking*, 1:324.

^b Report of Bank Commissioners, New York, 1842; Report of Bank Commissioners, Connecticut, 1846.

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tively extend larger discounts and thus earn greater dividends, the mother bank would be obliged to curtail its accommodation in order to be prepared to redeem the notes of its subordinate offices.^a In the charter of the First United States Bank permission was given to the directors to establish offices of discount and deposit only in any part of the United States, but it was not supposed at first that this permission would be taken advantage of. The directors, however, promptly decided to open branches at New York, Boston, Baltimore, and Charleston, and the number was afterwards extended. The bank did not take the notes of its branches, and this was one of the grounds of criticism in 1811.^b

In the charter of the Bank of Pennsylvania, 1793, provision was made for the establishment of branches anywhere in the State, subject to the consent of the town or borough; several were put in operation, but most of them were discontinued by 1810. In that year a law was enacted requiring the central bank to be responsible for all notes issued by the branches.^c In 1809, the Philadelphia Bank was authorized to have eight branches, and established four. Their business exceeded that of the parent institution and gave it much concern; ultimately they were found unprofitable, and by 1817 arrangements were made to dispose of them.

Bryan, in his "History of State Banking in Maryland," refers to the influence which the Scotch system had upon the development of banking in Maryland, and to

^a Matthew Carey, Letters to Doctor Seybert, p. 19.

^b Ibid., p. 58.

^c Laws of Pennsylvania, 1809-10, p. 27.

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this he attributed the introduction of branch banking in 1804. It had, however, but little development; no bank had more than two branches and only a few had any. Attempts were made to extend the system, but they were not successful.^a In Delaware the Farmers' Bank of Delaware had three branches.

The Bank of Richmond in Virginia, by its charter, 1792, was authorized to establish offices throughout the State with separate directors or agents. It was, moreover, provided that any town holding 300 shares should have the right to an agent, who should forward proposals for discount to the directors.^b The system of branches was continued in that State for many years.^c

From the beginning branch banking was the rule in North Carolina. In 1860 there were 16 banks and 26 branches in different parts of the State. The constitution of the State of Alabama, 1819, provided that state banks might establish branches when authorized by the legislature; provided, however, that not more than one be created in any one session. Although the state bank was chartered in 1823, no branches were organized until 1832; four were finally established, but their operation led to abuses. They were run too independently of the parent bank; discounts were extended, and the circulation was inflated beyond a conservative limit, the State being bonded for their issues.

^a Pages 15, 83, 85.

^b Laws, Va., Ch. 77, sec. 24.

^c Farmers' Bank of Virginia, 1812, to have six branches; Laws, Va., 1836-37, ch. 83, sec. 2; Laws, 1849-50, ch. 59.

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In 1838 the Union Bank was chartered by Mississippi and expressly authorized to establish branches, so that loaning facilities could be brought near to residents in different parts of the State. The bank on a technical excuse did not create the branches expected under the law, and consequently brought upon itself the criticism of the legislature.

In Missouri the charter of the Bank of St. Louis, the first institution organized in the State, permitted branches, provided they were 50 miles from St. Louis and the same distance from each other. No branches, however, were ever created. The charter of the Bank of Missouri, 1817, provided for the establishment of a branch for discount and deposit only in a county which subscribed for \$40,000 of the total capital of \$250,000.

The constitution of Indiana, 1816, forbade the establishment of a bank unless it should be a state bank with branches. When the State Bank of Indiana in 1833 was under consideration the chief point of dispute was the number of branches. The bill fixed this at 10; attempts were made to reduce it to 5 on the supposition that the fewer the branches the less mischief there would be. Ten branches, however, were ordered; for most purposes they were independent banks, subject to a certain control by the State Bank. The latter was really nothing more than a board chosen by the legislature, consisting of a president and four members, besides one member chosen by each of the branches, who had certain restrictive and supervisory functions with little power of initiative; and

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banking powers were exercised through the branches.^a The board of directors could limit and control the discounts of a branch after they reached one and one-fourth times the paid-in capital; they could suspend a branch and close it; could equalize the public deposits in the branches; were required to examine each branch once in six months; could require reports; could call on them to make up any deficiency in the assets of an insolvent branch; could regulate the dividends so as to prevent impairment of capital and secure a surplus fund of one-sixteenth the capital; and could print the notes for all the branches. Subject to these restrictions, branches were free to conduct their business without control. Each branch elected its own board of directors except the three appointed by the state board, and the profits of each were independent of all the others. The system did not work well; it was complained that the parent bank exercised but a loose supervision over its branches and "used toward its branches the language of a weak, indulgent, and incapable parent who scolds her children, indeed, and threatens and then lets them do pretty much as they please." The independence of the several branches in the State Bank was partly attributed to the fact that conditions were different in different parts of the State. Some of the branches were in river towns, some in the interior, one on a lake; the southern part of the State was settled by people from the South and the northern by

^a Laws, Indiana, 1834, ch. 7, secs. 2-3, 24; W. F. Harding, *Journal of Political Economy*, December, 1895, p. 4.

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those from the East. The result was a diversity in business customs and standards.^a

Although the branch system did not obtain a foothold in the North, banks attempted to extend their operations to a distance through agents. In 1837 several banks in Connecticut established agencies in different parts of the State for the purpose of making discounts, but the bank commissioners claimed that these were virtually branches which had not been recognized by law and should be prohibited, or each branch should be made a separate and distinct institution.^b

In 1836 the bank commissioners of Rhode Island noted that though discounts were generally made at the office of the banks, in some cases there was a committee which made loans elsewhere. The legislature thereupon promptly passed a law forbidding any bank to have an office or agency for discount in any place other than the office of the bank, except by express permission.

Massachusetts also condemned the practice, the law reading: "No loan or discount shall be made, nor shall any bill or note be issued by such bank, or by any person on its account, at any other place than at its banking house."^c Notwithstanding this prohibition, some banks violated the spirit if not the letter of the law. In 1852 the bank commissioners severely condemned existing practices: "Banking institutions have a locality to which their operations are designed to be confined. It is a perversion of such design if the officers are sent into the money market

^a W. F. Harding, *Journal of Political Economy*, December, 1895, p. 9.

^b Reports of the Bank Commissioners, Conn., 1837, 1838.

^c Revised Statutes, Mass., ch. 36, sec. 8.

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in other places in pursuit of paper which, under the form of exchange, will give a higher rate of interest than it would be prudent for them to exact of the business community in their own neighborhood; it is an interference with the rights and interests of other banks, and the practice is frequently attended with loss on account of ignorance of the true character of the paper. The increased facilities of communication have a tendency to concentrate business in the metropolis. Managers of banks in the country, established for local convenience, should be at all times aware that to discount paper, receive checks, and exchange their bills through an agency in the city is an infringement upon the foregoing statute."^a

In the following year the bank commissioners found it necessary to take a more decisive action. Several banks had been chartered in towns in the vicinity of Boston where the local business was not large. In order to employ their funds more profitably, the banks opened offices in State street, Boston, and at stated hours the cashiers were in attendance to receive deposits, pay checks, discount notes, and indeed do all the business of the bank. In two or three cases the business done in the city was greater than that performed at home. In consequence of this the bank commissioners issued a positive prohibitory order and threatened an injunction on one or two banks which were disposed not to yield.^b

The free banking act of New York of 1838, amended in 1848, expressly prohibited the establishment of branch

^aSecond Report of Bank Commissioners, Mass., 1852, p. 8.

^bBankers' Mag., 1853, 8:437.

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banks, due to a fear that banks in large cities might monopolize the profits of note issue by organizing branches in small inaccessible towns and thus throw obstacles in the way of easy redemption of bills.^a

XXII. RIGHT TO CARRY ON A BANKING BUSINESS.

During the earlier years of banking the business was frequently carried on by private individuals and unincorporated associations, whose operations extended to the issue of notes as well as to the making of loans and the receiving of deposits. Massachusetts was the first State to place restrictions on such private enterprise. In 1799 a law was passed forbidding anyone to join any association to do banking unless authorized by law; and a penalty of \$1,000 was imposed to be recovered by anyone who issued an action for debt, one-half to go to his own use and one-half to the State, while the notes of such an association were void.^b New Hampshire, also, in the same year prohibited private banking. Rhode Island, in 1805, forbade the issue of notes by private parties. As late as 1826, however, the question of removing restrictions came up, but a legislative com-

^a "Certain persons acting under the provisions of that law had set up their so-called principal offices in obscure villages of the backwoods while issuing their notes and attending to such other business as came in their way in the important cities. As they were thus able to evade or delay redemption at city offices by referring holders of their paper to the remote counters at which alone it was payable, or later might refuse to redeem in Albany or New York except at a discount, the legislature sought to mitigate the scandal by requiring that the usual business of a "free bank" should be transacted at the place named in its certificate." R. M. Breckinridge, *Sound Currency*, 6:8; see *Laws of New York*, 1838, ch. 260; 1840, ch. 202, 363; 1848, ch. 340.

^b Acts, Mass., 1799, ch. 32.

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mittee reported adversely; attention was called to the great number of failures of private banks in England in 1814 and 1815, and as the community had become accustomed to regard existing currency with confidence and it was held unwise to risk the possibility of a flood of insecure notes.

In 1804 New York forbade all unincorporated companies from doing a banking business,^a but this prohibition did not forbid individuals or incorporated institutions from engaging in banking and issuing notes. Insurance companies, aqueduct associations, and many individuals, such as tavern keepers and merchants, issued notes in denominations as low as 6 cents. During the war of 1812 this became a serious evil.^b The act of 1804 did not owe its origin to any new public policy, but to the desire of capitalists already interested in banks in New York City to prevent the Merchants' Bank from continuing business without a legislative enactment. In 1818 a more sweeping law was passed: "No person, association of persons, or body corporate, except such bodies corporate as are expressly authorized by law, shall keep any office for the purpose of receiving deposits or discounting notes or bills, or issuing any evidence of debt to be loaned or put in circulation as money; nor shall they issue any bills or promissory notes or other evidences of debt as private bankers for the purpose of loaning them or putting them in circulation as money, unless thereto specially authorized by law."

^a Laws, N. Y., 1804, p. 476.

^b Knox, *History of Banking*, p. 398.

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It will be observed that this law went far beyond the prohibition of the issue of notes, for it forbade receiving deposits or making loans. The reason for this legislation was largely due to the increasing operations of a private bank managed by Jacob Barker, who was rapidly extending his business and encroaching upon the profits of the chartered banks; these, therefore, endeavored to cripple his activity.^a It was difficult, however, to stamp out a non-banking medium of circulation. In 1824-25 the legislature chartered several loan companies which issued bonds and passed them off as money, and this addition to the volume of circulating paper was regarded as one of the causes which led to the cotton speculation of 1826. There was moreover continued discussion as to the wisdom of such absolute restriction, and according to Gallatin, the act of 1818 had no other effect than to deter prudent capitalists from engaging in banking business, and this increased interest rates.^b Legislative committees in 1825 and 1826, recommended repeal on the ground that monopoly sheltered abuse; the operations of unincorporated persons could not be conducted with so much concealment; private bankers subject to unlimited liability would be cautious; restriction tended to accumulate capital in New York City, and deprived the farmer and manufacturer in the interior of loaning facilities; and the system of charters did not prevent dishonesty. Although a charter might originally be placed in safe hands, the stock was transferable and could pass into the hands of irresponsible

^a Jacob Barker to the Public, 1819.

^b Gallatin, Writings, 3: 350.

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persons.^a In 1837 the restraining law was repealed, thus leaving every citizen in a position to pursue the business of banking under the general law. It was followed by the creation of a large number of private banking houses in New York City, which received deposits, discounted notes and bills of exchange, and dealt in coin and bullion.^b

The change in policy excited much opposition, and the Attorney-General denounced the measure as inexpedient and unconstitutional.^c By the act of 1838, providing for the issue of notes based upon deposits of mortgages and stock, private persons and partnerships, which were not bankers at all, could issue circulating notes. For a time there was uncertainty as to the construction of this law, as it was difficult to reconcile it with other laws dealing with corporations. One decision announced that private persons or companies could not issue negotiable obligations, and that if issued, they were under no obligations to redeem them; the construction extended even to bonds.^d This opinion, however, was condemned by a higher court on the ground that the legislature never intended, in its efforts to suppress offending banks, to destroy all the bills which they put into circulation.^e The reversal did not remove popular uneasiness. In one instance, the supreme

^a Report of Committee on Judiciary, N. Y., Jan. 31, 1825; Report of Committee on Banks and Insurance Companies, 1826.

^b Report of Superintendent of Banking Department, N. Y., Jan., 1860, p. 5.

^c Senate Document, N. Y., 1835, No. 4, p. 13; Report Assembly Document, 1837, No. 303, p. 7.

^d *Safford v. Wycoff*, 1 Hill, 11.

^e 4 Hill, 465.

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court set free a person who had counterfeited the bills of a free bank,^a but this decision was also overruled.^b

New Jersey in 1815 forbade unincorporated institutions from doing a banking business under heavy penalty.^c Pennsylvania, in 1808, forbade banks incorporated under laws of other States to do business within her boundaries, and two years later, unincorporated associations were forbidden to issue notes, make discounts, or receive deposits, but the law was of little force, particularly in the interior. There was a scarcity of specie and as the state banks did not issue notes under \$5, there was a lack of circulating medium. Notes were consequently emitted by bridge and turnpike companies.^d The Girard banking house, a private bank which began business in 1812, issued notes and this raised the question whether the other Philadelphia banks would receive them. A committee of these institutions decided that since the laws of Pennsylvania discouraged, if they did not prohibit the circulation of notes of unincorporated banks, Girard's notes should not be received either in payment or on deposit. Later, however, they yielded and received the notes.

In Maryland many of the early banks were started as private institutions, but in 1810 an act was passed to prohibit persons from associating with the purpose of forming a banking company without first applying for a charter. Each subscriber to such an association was liable to a forfeit of \$100 and the commissioner who under-

^a *Debow v. People*, 1 Denio, 19.

^b *Gifford v. Livingstone*, 2 Denio, 380.

^c Pub. Acts, N. J., 39 Ass. 2 sess., p. 13.

^d Sumner, *History of Banking*, 1:44.

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took to receive subscriptions to a fine of \$2,000. The law was disregarded and there is no evidence of the imposition of the penalty.^a In 1817 another law was passed to the same effect, but this again did not prevent individuals from carrying on a banking business.^b

Virginia in 1805 made it unlawful to pass a note of any unchartered bank. In 1816 unchartered banks were declared illegal and their notes null and void; a fine was imposed for signing such a note and the holder of a note under \$1 could recover \$5 from the issuer or signer. In 1820 new penalties were inflicted with imprisonment from one to twelve months for individuals and a fine of \$50 for corporations. A fine of from \$10 to \$100 was imposed for bringing such notes into the State for circulation, and a fine of \$10 for offering to pass them. In 1848 trading by members of an association in the manner of a bank, issuing or circulating notes or other instruments of an unchartered company was made punishable by a fine of from \$100 to \$500 and imprisonment.^c

North Carolina forbade private note issues in 1816. Georgia, in 1815, imposed a tax of 8 per cent on all bills then circulated by unchartered banks and 20 per cent on all subsequent issues.^d In the following year it forbade any unincorporated association from issuing notes of \$2 and over, and in case of violation, the holder might recover 125 per cent. For notes less than \$2, the holder might recover three times the value.^e Florida, in 1824,

^a Bryan, *History of State Banking in Maryland*, p. 42.

^b *Ibid.*, 31.

^c *Laws, Va.*, 1847-48, ch. 10, secs. 18-21.

^d Knox *History of Banking*, p. 575.

^e Sumner, *History of Banking*, 1: 87-88.

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passed an act imposing a penalty of \$50 on any one bringing into the Territory with intent to circulate, "any bills and notes in the likeness of bank notes, which said bank notes are, or have been, issued by any private individuals or private unincorporated companies in the United States."^a

In Alabama, owing to the rapid purchase of public lands, the Territory was drained of good money. This led, therefore, to the issue of small notes, called "change bills" by corporations, firms, and even individuals. The legislature consequently sought to restrict this abuse and in 1818, enacted that all such notes for a sum not exceeding \$1 were to bear interest at 100 per cent per annum from date of issue.^b This became a dead letter, as did much subsequent legislation of the same character.

In Ohio, before 1815, there were various concerns carrying on a banking business without charters. Some of these were swindling operations and others engaged in business in good faith and afterwards became chartered institutions. In many instances they issued notes until the legislature resolved to put an end to opportunities for abuse, and passed an act prohibiting the unauthorized issue of circulating^c notes. There was a penalty of a year's imprisonment as well as a fine, and contracts with persons or firms engaging in unauthorized issue were void. This was the first of a long list of laws directed against unauthorized bank notes.^d Agents of banks chartered by other

^a Act of Dec. 22, 1824.

^b Territorial Acts, Ala., 2d sess., Nov. 17, 1818.

^c Laws of Ohio, 1815, 13:152.

^d Laws of Ohio, 1816, 14:10.

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States were subject to fine and denied the privilege of enjoining the courts; and anyone interested in such a bank was made personally liable to any noteholder. These restraining laws apparently did little good. It is stated that in Zanesville, in 1818, there were more than 30 kinds of paper passing from hand to hand; besides bank notes, there were shinplasters issued by bridge, turnpike, and manufacturing companies, city and borough authorities, tavern keepers, and shoeblacks, ranging from 3 cents to \$2.^a With few exceptions, these notes were of little value.

Kentucky, in 1817, forbade the issue of notes over \$2 by unauthorized associations, under penalty of ten times the note; everyone who passed the note was liable to the same penalty. This act, however, was only temporary in its operation. Indiana, in 1815 (Dec. 26) subjected any person issuing or passing an unauthorized note to a fine of three times the amount, with liability to the holder.

In 1830, practically all States had confined the right of issue to incorporated banks. The solitary exception was Girard's Bank in Philadelphia. Congress, however, had not restricted the issue of notes by the city of Washington and there was still a small amount of paper in circulation issued by the State of North Carolina.^b Gallatin's statement did not, however, hold good for subsequent years. Under the cover of suspension of specie payments and the looser laws of the new Western States and the nonenforcement of the laws already in existence in the eastern section, a very considerable amount of fractional bills issued by

^a McMaster, *History of the United States*, 4:317.

^b Gallatin, *Writings*, 3:264-265.

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individuals and business firms were at one time and another put in circulation, oftentimes for the purpose of supplying the want of small coin, due to the disappearance of silver after its undervaluation at the mint by the coinage act of 1834. A writer in the Merchants' Magazine in 1853 stated that in the interior a large batch of private shimplasters had been issued, to the amount of between \$1,000,000 and \$2,000,000, which found a ready circulation.

XXIII. LOANS AND DISCOUNTS.

The subject of loans and discounts may be treated under the following headings:

(a) The procedure followed in applications for loans and in passing upon them by the directors or committee of management.

(b) Character of security.

(c) Length of the loans.

(d) Renewals of loans.

(e) Amount of loan to any one person.

(f) Loans to directors.

(g) Partiality in making loans.

(h) Restrictions upon residents and nonresidents.

(a) *The procedure followed in applications.*

The by-laws of each individual bank commonly provided for the receiving of discounts either on one or two stated days in the week, and requests for loans were to be left on one day to be passed upon by the management of the bank on the following day. The Bank of New York, 1784, made its discounts on Thursday, the offerings to be left under a sealed cover on Wednesday morning.

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It was the rule of the United States Bank, 1791, to receive offerings on Mondays and Wednesdays, settle them on Tuesdays and Thursdays, and make them known the succeeding days.^a The Bank of Pennsylvania, 1793, prescribed that paper offered for discount should be delivered on Tuesday and Friday and passed upon the next succeeding days.

By the rules of this bank no discount could be made without the consent of three-fourths of the directors present.^b The Bank of New York, early in the century, voted that no notes be discounted between meetings of the board, except in special cases upon judgment of the president, and then not exceeding \$4,000. Under the rules of the Hartford Bank, 1792, all questions relating to discounts were determined by ballot, and if two voted in opposition the loan was not granted. No reason was to be given for the refusal.^c In 1819 it was agreed that no name which had appeared as a drawer, acceptor, or indorser on unpaid paper, should be given consideration in any proposal for a loan. A copartnership desiring favor must declare the names of its members,^d and one partner could not be accepted as an indorser for another. By an act of Vermont in 1840, no loan exceeding \$50 could be made without the approval of a majority of the directors. The charter of the State Bank of Indiana forbade the directors to vote on loans in which they were interested, and on

^a Leach, the Girard National Bank, p. 17.

^b Same in Virginia, Laws, 1836-37, ch. 82, sec. 6; Second United States Bank, 1816; By-laws, Girard Bank, 1832; Branch of the Bank of the State of Alabama, 1832; Franklin Bank, Cincinnati, 1833.

^c Woodward, The Hartford Bank, p. 64.

^d Ibid., 125.

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all applications for \$500 or upwards there must be five concurring votes out of seven.

(b) Character of security.

1. *Loans on pledge of bank stock.*—Loans on the pledge of bank stock were made at an early date largely to aid stockholders in satisfying the loose charter requirements in regard to the paying in of capital. Such loans were made not only to assist the subscribers, but also in the ordinary business of the bank to furnish easy accommodation to the owners. For a time there does not appear to have been any special opposition to such loans, but abuse arose in evading requirements as to paying in of capital, and, secondly, in the special favors which stockholders obtained, when banks came to be established to confer special rather than general benefits. Bank stock was naturally regarded as excellent security, and so it was not unusual for banks to permit loans to be made to stockholders upon pledge of bank stock on single-name paper instead of the usual requirement of two responsible names. Such a provision is to be found in the by-laws of the Farmers' and Mechanics' Bank of Philadelphia, 1809. The by-laws of the Bank of the Valley (Virginia) allowed loans to stockholders on pledge of stock without an indorser, for three-fourths of the amount paid in.

The by-laws of the Second United States Bank, 1816, also provided that if stock of the bank, or United States stock or other such property approved by the board, were pledged, one responsible name was sufficient. Upon its organization the operations of this latter bank in aiding the stockholders to pay their second installment due on

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the capital through loans on bank stock became a scandal. The directors in December, 1816, gave express authority by resolution for such loans and in the following year (Aug. 26) authorized stockholders to borrow on their stock at an advance of 25 per cent on the par value thereof.^a

Later there was so much abuse of such loans that some States passed laws forbidding or limiting the practice. Massachusetts, for example, in 1829, in a general banking law forbade loans on pledge of bank stock for more than one-half of the capital paid in. The charter of the Bank of Florida, of the same year, forbade any such loan. The same provisions are to be found in the charters of the Franklin Bank of Cincinnati, 1833, and the Louisville Bank of Kentucky, 1833.

The bank commissioners of Connecticut, beginning with 1837, reported against this practice. They declared that banks were not established for the exclusive benefit of stockholders, but they were pleased to report that there was only one bank in the State where these loans were excessive. In 1841 they recommended that no stock note should be discounted for more than three-fourths of the value of the stock; that none should run for more than four months, and all such notes should be paid in full at maturity. Vermont, by an act in 1840, expressly prohibited such loans. The charter of the State Bank of Indiana forbade loans on bank-stock collateral. In 1839 the bank commissioners reporting on the State Bank of Illinois stated that the indebtedness to stockholders was

^a For further details see Dewey, *The Second Bank of the United States*.

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large, amounting to one-fourth of the total. Nearly two-thirds of the amount which had been paid in by private stockholders had been loaned back to them. In the following year the legislature prohibited such loans.

2. *Accommodation paper.*—A very considerable part of the loans which were made during the earlier period of banking were accommodation loans. This was in harmony with the prevailing opinion that banks should serve all classes by an advance of credit irrespective of the condition that such credit could be promptly liquidated.

In a contemporary report the following distinction was made between accommodation paper and business paper: "When an individual simply wishes to borrow money and offers his notes with security to the bank, it is treated as an accommodation subject to the customary call and renewable. When a party holds a note given to him by another for property sold and indorsed and sells it to the bank, payment is always presumed and expected at maturity, and it is termed a real transaction and the security, business paper." According to Matthew Carey there were two general varieties of accommodation paper, "draw paper," and "extra accommodation paper." ^a The former carried on its face the evidence of its being fictitious by the indorser transferring his claims in the proceeds to the drawer. The extra accommodation notes were drawn to appear as if issued in a bona fide commercial transaction for value received. According to Holdsworth, business conditions in Pennsylvania were such as to make a considerable use of accommodation paper impera-

^a Carey on Banks, Appendix, p. 2.

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tive. The importing merchant sold his merchandise largely to country storekeepers at the nominal credit of six months, but generally he could not obtain payment under twelve months or even longer. These accounts with country merchants were open-book accounts, very little being given in payment. The retail shopkeeper was in much the same situation as the wholesaler. He bought his stock of goods on a six months' note and sold the bulk of it on accounts current to people who did not expect to settle oftener than once a year. How then, were the wholesale importers and the large merchants to meet their obligations and to replenish their stock? They received in payment little cash or bona fide paper. To secure bank credit they had to have recourse to accommodation paper.

Some idea of the extent to which the handling of accommodation notes went on may be had from the incident related by Matthew Carey, himself a bank director and merchant in Philadelphia, at the close of the war with England. There were three large package sales of merchandise belonging to the merchants of Philadelphia during the summer months of 1815, amounting in all to \$1,515,000. The auctioneers made payment as follows: Bank drafts, \$665,900; several notes of sixty days ranging from \$10,000 to \$50,000, amounting to \$500,000; the balance in notes of the purchasers of the goods. These auction notes were all discounted at the different banks. Carey declared that these notes at one time amounted to over \$1,200,000.

As time went on, and it was found that in order to secure redemption of circulating notes it was necessary to

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have assets easily available, accommodation paper fell into disfavor in the larger cities. In 1832 the charter of the Girard Bank in Philadelphia forbade the discounting of a note which on its face bore the evidence of accommodation paper. Country banks, however, still favored this form of investment of funds. In 1833 less than half of the discounts of such banks in New York could be called business paper. In New England there was a more marked change; the bank commissioners of Massachusetts in 1840 noted with approval that banks were reducing their accommodation notes; and by 1845 nearly all bank discounts in Connecticut were on business paper. By the middle of the century, in the larger cities, accommodation was rarely offered and more rarely accepted. This change did not escape criticism. The bank commissioners of Massachusetts in 1840 thought that country banks might make exceptions in favor of accommodation notes, for such loans frequently proved serviceable to their communities, and in Connecticut the bank commissioners regretted that a worthy class of borrowers was deprived of advantages to which they were entitled.^a

In the South and Southwest public sentiment was divided. At times it was recognized that accommodation notes were insecure and tied up the resources of a bank so as to seriously embarrass it. In 1836 the president of the Bank of Kentucky urged his board of directors not to make any further loans, except those payable at maturity, and also to get "clear as soon as practicable of the discounted notes, styled accommodation paper."^b When

^a Report of Bank Commissioners, Connecticut, 1841.

^b Duke, History of Bank of Kentucky, p. 46.

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banks, however, attempted to restrict the volume of accommodation loans and turned to bills of exchange for investment, they were severely criticised, on the ground that they sought an extra profit instead of devoting their funds to the assistance of local and needy borrowers. For example, a legislative committee of Kentucky in 1840 complained that the banks by falling into the practice of doing a large business on accommodation notes instead of business notes caused great embarrassment to the banks without furnishing any equivalent advantage to the country. It was highly necessary that the banks should do an exchange business in order to make it possible to pay specie outside the State. In Georgia the Central Bank by its charter was authorized to loan on accommodation paper and forbidden to demand more than 20 per cent of the principal at the end of a year, unless necessary, and in 1829, Dec. 19, the charter was amended requiring the bank to discount the notes of debtors to the State. The Bank of Indiana also, in 1839, noted with regret that its branches made extensive loans on accommodation paper, on much of which calls could be made for only 10 per cent or less per annum.

Akin to loans on accommodation paper was the practice of loaning on memorandum checks and overdrafts. In 1837 the bank commissioners of Massachusetts reported that they found checks for small amounts in many banks, and in a few for large sums. The latter were generally secured by stock lodged as collateral. This kind of accommodation was becoming unpopular, but its existence was again referred to in 1841.

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3. *Loans on real estate.*—As a rule, banks made loans on real estate. As already stated, in some States banks were obliged under their charters to loan a certain portion of their capital to farmers, and this obligation was imposed upon city banks, as in Boston. Gradually such loans were regarded by the sounder banks in the North with disfavor, as they ran for too long a time and it was difficult to secure prompt settlement at maturity. In 1820 a report was made by the State Bank in Boston in regard to loans on real estate: \$263,460 had been thus loaned to 719 persons; 639 of these had paid a part or the whole, amounting to \$127,751; 80 of them had paid no part of the principal, amounting to \$30,081; and the balance due from 639 persons was \$105,627.^a Efforts were made to close up these accounts, but some were outstanding as late as 1839. At times city banks were drawn into loans on mortgages, particularly during periods of real estate speculation. In a report made to the legislature of New York in 1831, it was stated that nearly \$50,000,000 was loaned in New York City on mortgage and the greater part of it at 7 per cent.^b In 1836 the bank commissioners of that State reported that banks had, under the guise of business paper, supplied credit to those engaged in real estate speculation. According to Clibborn,^c it was the general practice in Cincinnati to give accommodation to merchants or dealers in real estate, such as town lots and houses in cities, rather than to the discounting of real bills of exchange, which was but

^a Stetson, *An Historical Sketch of the State Bank*, p. 44.

^b Niles, 40:185.

^c *American Prosperity*, 1837.

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a minor branch of their business. The banks encouraged the renewal of these notes, and by taking mortgages on the property would finally come into possession of a large part at their own price. There were, indeed, two such sales of nearly the whole city by the United States Bank. In a settled population such a system could not exist long, but in American towns, where there was a continual change, experience was lost, and the practice could easily be repeated.

In the South banks were expressly organized to loan on real estate. The Planters' Bank of Mississippi, 1830, could make loans secured by mortgage up to one-third the value of the property. The Union Bank of Louisiana was essentially a land and slave bank and the charter provisions carefully prescribed the amounts which could be loaned on lands, brick dwellings, slaves, etc. The Commercial Bank of New Orleans, 1833, could also loan on lands and slaves secured by mortgage. Property in the city must be improved and plantations be in full state of cultivation. The Union Bank of Florida (Tallahassee), 1833, was also authorized to make loans on lands and slaves. In 1836 the Real Estate Bank of Arkansas was chartered; 127,500 acres of land were mortgaged, of which only about 14,000 acres were under cultivation.

The management of the Bank of the State of South Carolina in 1843 referred with satisfaction to its success in making loans on bonds and mortgages and for longer periods than business paper would run. They admitted that not all of the capital and credit should be so

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invested, but a considerable part could be safely and profitably thus loaned. This was seen during the suspension in 1839; of the seven banks in Charleston, six were purely commercial, rejecting bonds and such securities; of these, five suspended specie payments, while the Bank of the State of South Carolina, which loaned on real estate, paid in specie all its notes as presented. Although such loans were slower in payment and the profits in business founded on lands and slaves of the planter and mechanic and tradesman were not so large, all the property was visible and could not be easily wasted without detection, and the losses and risks were smaller.

Maryland introduced at an early date, in the practice of the Farmers' Bank at Annapolis, a feature borrowed from Scotch banking, known as the system of cash accounts. An account of this sort might be opened on application of any farmer, mechanic, or manufacturer for sums from \$100 to \$1,000, whereby the borrower might draw or pay in any sum not less than \$50 at any one time and on which settlements were to be made semiannually, the party drawing the cash to pay interest for what he might owe at 6 per cent per annum and to be allowed interest on all sums returned from the time of payment. The party opening an account had to give good personal or real security; the directors were not obliged to lend money on such cash accounts to a greater amount than one-fifth of the capital. The object of the practice was to aid the farming interest, and was practically but another method of loaning upon real security, since most of the bank's patrons had little other available security. An attempt

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was made to introduce this method into the business of some of the Baltimore banks.^a

Crawford, in 1820,^b severely criticised loans to farmers. He admitted that the establishment of banks in agricultural regions had greatly improved the general appearance of the country; comfortable mansions and spacious barns had been erected; lands had been cleared and reduced to cultivation; farms had been stocked and rendered more productive by the aid of bank credits, but they had been accompanied by the ruin of the owner. The farm, with its improvements, proved unequal to discharge the debts incurred in its embellishment. So general was this distress that state legislatures were compelled to enact relief measures and stay-laws to rescue their fellow citizens from the inevitable effects of their own indiscretion. Of similar import was the opinion of the governor of Georgia in his message to the legislature in 1823; the operations of banks were ruinous when introduced into the interior of the country, and banks should be created only in those places where surplus products of the State were carried to the market.^c

4. *Loans on Merchandise*.—Some banks in the larger eastern cities made a special practice of loaning to merchants on merchandise. For example, the Bank of New York, which was chiefly a merchants' bank, beginning with 1804, made advances on merchandise, and appointed a special officer to inspect and appraise the goods offered as security; this appraiser received a commission of

^a Bryan, *History of State Banking in Maryland*, pp. 37-38.

^b Finance, 3:498.

^c See Niles, 35:346.

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one-half of 1 per cent of the loan, which was paid by the borrower.

In Pennsylvania loans on merchandise came into general use during the embargo period. Owing to commercial embarrassment, the banks came forward to tide over the delays which took place in realizing on importations. A resolution of one of the Philadelphia banks, adopted November 28, 1808, provided that the payer and indorser of a note and the drawer and acceptor of a bill presented for discount must be competent to meet their engagements; that to insure this, an amount of property not of a perishable nature, should be held either by the indorser, acceptor, or such other person as might be approved of, sufficient to cover the amount loaned; that after a deposit had actually been made, those who received it must give ample proof and hold themselves bound not to part with it until the bank should express its assent. In either case, the property must be insured against fire. As noted by Holdsworth, the historian of the Bank of Pennsylvania, the use of the collateral loan, thus begun in adversity, was in after years greatly extended in prosperity.

In the Southern States banks made extensive advances on produce on the ground that cotton, tobacco, and sugar were staple commodities which, if necessary, could be kept until a market was found. Later, however, when there were violent fluctuations in prices, the banks in that section became seriously involved; particularly was this so during the period of cotton speculation in the thirties. In Alabama the directors of the State Bank of Alabama, in 1837, in order to increase their stock of specie, decided

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to make loans on cotton so as to secure exchange facilities abroad. Anyone with a supply of cotton on hand might have it valued, and on delivering it into the charge of the bank receive an advance of not more than 25 per cent of the value, and then give his note for the amount received, payable in nine months. The bank then shipped the cotton at the risk of the owner, who had the right to limit the selling price until the cotton had been in port five months. The proceeds of the sale were placed to the credit of the note and the excess paid over to the owner of the staple. In case the citizen was greatly pressed for money and his cotton was not ready for delivery, the bank might make him advances on his executing a written pledge to deliver the cotton at some future date to the bank agent in Mobile, in amounts sufficient to repay the funds loaned.

The State Bank of New Orleans in 1836 voted that whenever sugar or cotton were deposited in warehouses and insured, the notes of the proprietors should be discounted for two-thirds of the cash value. In order to avoid indorsement on notes and bills of exchange, credit should be opened to those who could furnish mortgages on real estate, not to exceed two-thirds of the cash value offered.

The Mississippi Union Bank made loans on cotton; the planter executed his note with indorsers to an amount equal to the number of bales at \$60 each. The cotton was shipped under the control of the bank and sold in such markets as the planter desired; the benefit of the exchange went to the planter and no charges or commissions went

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to the bank.^a In 1837 from two-thirds to three-fourths of the loans of the Northern Bank of Kentucky were upon notes and bills disbursed by drovers in the purchase of live stock and driving the same to market, and by others in aid of agriculture; fifteen-sixteenths of the capital of the bank and its branches was employed in agriculture. Of a somewhat similar character was the business authorized by the charter of the Bank of St. Louis, 1813, whereby the bank could receive and hold as security for loans and discounts, lead, or barter, or fur, or other property, provided it was left in the care, possession, and control of the bank. In 1839 the State Bank of Illinois was criticised for its connection with trade in lead and other commodities; \$507,000 had been advanced on lead alone. This was regarded as contrary to the spirit of the charter, for the bank had been created for the common good of all without reference to locality or particular pursuits.

5. *Loans on stocks.*—There was a long-continued objection to temporary loans on stocks for collateral security, for such loans were more commonly advanced to brokers, who were generally regarded as engaged in speculative operations entirely foreign to the primary purposes for which banks were established. A legislative committee of New York in 1837 criticised the banks for making temporary loans on securities. It was recognized that often the motives for such loans were good, for this practice enabled banks to be prepared at a moment's notice to meet any contingency; on the other hand, it made it possible for brokers to secure funds with which to specu-

^a Report of Bank Commissioners, Mississippi, 1838.

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late. The committee therefore recommended that no bank be allowed to take stocks in hypothecation. As securities at that time were not sound or stable, the commissioners held that such loans were not more available than those which were made on common paper; the stocks took the place of individual liabilities, while the money went to furnish other States with capital. Too much capital was thereby absorbed by the "fancy" stocks, both of New York and other States.^a Such loans, however, increased until in 1855 an unusually large proportion of the loans and discounts of the New York City banks were loans on call.^b This change aroused criticism; a writer in Massachusetts stated that it was a common weekly occurrence for bank officers to appear at exchange or on the curbstone for the purpose of negotiating with other banks or bankers, at the same time refusing their own customers money for good paper for the proper transaction of business in their own localities. City banks borrowed of the country banks, a practice of very doubtful utility.^c The bank commissioners of Massachusetts in 1855, thought that the system of demand loans was one to be deprecated, for it put too great a strain upon the community; banks had better substitute for demand loans, paper so timed that it will turn up at proper intervals to relieve the circulation without surprising the public.^d In 1858 the governor of Connecticut recommended that banks be prohibited from making loans on call.^e

^a Assembly Document, N. Y., No. 328, May 11, 1837.

^b Merchants' Magazine, 33:340.

^c Silex, Letters on Banks and Banking, 1853.

^d Fifth Report of Bank Commissioners, Mass., pp. 74-75.

^e Merchants' Magazine, 39:97.

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6. *Exchange*.—During the first quarter century of banking in the United States banks did not seek to gain a special profit by dealings in bills of exchange. According to Raguet,^a "The discounting of notes or acceptances payable on the spot was the sole mode in which the capital and credit of the banks were formerly employed, and if by way of accommodating their customers they occasionally discounted a note or acceptance payable at a distant place it was always done upon the spot, the banks not calculating upon any profit in the way of exchange, but relying on getting their money back again by supplying another customer with a check or draft at par." Ordinary exchange transactions between different cities and States were left to individual competition, which established the market rate. The Second United States Bank in 1817, however, entered upon the business of a dealer in domestic bills of exchange by buying and selling bills upon all points where its branches were located, upon terms that gave it a profit on the particular transaction, and this practice was responsible for the general custom which subsequently prevailed among banks.

During the life of the United States Bank exchange business was largely controlled by that institution. If it did not monopolize the business it practically determined the scale of rates which could be charged by local banks. With the downfall of the bank in 1836 and the closing of its branches the business fell into the hands of the local and state banks, and at once complaints were freely made in all parts of the country that these institutions were charging excessive rates.

^a *Currency and Banking*, p. 120.

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The term "exchange" was also applied to transactions which did not spring from a sale of goods, but was used whenever money was to be paid in a different place from that in which it was loaned. Banks here found an opportunity for imposing more than the legal rate of interest, and ordinary loans were frequently made to assume the character of an exchange operation. In many States this became a scandal so great that under the national banking law the right of charging exchange was granted only in the purchase, discount, and sale of a bona fide bill.

The bank commissioners of Connecticut, 1838, noted that there had been a great increase in the exchange business during the previous year and that the practice had been an evil of rapid growth. Connecticut banks discounted notes payable in New York and gave a draft for the net proceeds for which they charged from one-half to 3 per cent. This charge was far beyond the exchange expenses. It was consequently recommended that a tariff of exchange charges be adopted by the legislature or that a charge beyond exchange expenses be entirely prohibited.^a In 1855 a law was passed regulating exchange, but the state authorities complained that its spirit was evaded for the purpose of obtaining more than the legal rate of interest.^b

In Massachusetts the general banking law of 1829 provided that in discounting drafts or inland bills of exchange banks could charge over and above the rate

^a This recommendation was repeated by the bank commissioners in 1841.

^b Reports of Bank Commissioners, Conn., 1855, 1856.

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of interest only the then existing rate of exchange between the place where the draft was discounted and the place where it was made payable. In 1838 the commissioners reported that though the charges for exchange had not been extravagantly high many country banks demanded from one-fourth to one-half of 1 per cent for exchange on notes discounted which were payable in Boston. This was regarded as a questionable practice, for the country had no reason to make any such charge, since they wanted funds in Boston. The banks, however, defended the practice on the ground that they must compensate some city bank for the collection and redemption of bills in Boston. The legislature, by an act of April 25, 1838, made certain restrictions as to exchange, and in 1840 again passed an act for its regulation.^a

The law, however, was necessarily flexible and liable to loose construction and evasion,^b and the commissioners again reported that there was a great diversity of practice; some of the banks demanded no exchange upon paper payable in Boston, while others charged rates varying from one-fourth to 1 per cent; this was held unjustifiable, for such paper was almost universally preferred by banks; it was surer to be paid at maturity than paper payable at their own counters; and its payments placed their funds in Boston for the redemption of bills, at the least possible expense and hazard, with the least possible loss of interest. They also complained that the banks, when they made collections in their own vicinity for Boston or other banks, always made some charge for collecting and remitting the funds to Boston, on

^a Acts, Mass., 1840, ch. 94.

^b Second Report of Bank Commissioners, Mass., 1840, p. 15.

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the ground that they did not wish to draw upon their Boston funds.^a In 1842 the commissioners noted that this practice of charging by country banks on paper payable in Boston had been discontinued. However, the business was later revived; in 1851 it was stated that exchange was more generally charged than ever before and that institutions of long standing engaged in the practice.^b It was admitted by banks that paper had been framed for the purpose of receiving exchange.^c In 1860 attention was called to the fact that a large proportion of the paper on which exchange was charged was made payable in Boston or New York, and sometimes in the nearest large town, and occasionally even in places "ridiculously near." This exchange was found to exist between different parts of the same village, where it happened to lie upon the borders of two adjacent States; and one transaction was cited in which a bank director had made a note payable at another bank not half a mile distant across the state line, and paid one-fourth of 1 per cent exchange, when he was expected to pay the note at his own bank where it was discounted. The exchange was merely a respectable cloak to cover extra interest. Indeed, it was stated that in nine times out of ten where the objectionable exchange was charged, it was demonstrable that no exchange existed, or if it did exist, that it was in favor of the place where it was exacted.^d In 1862 one bank, by name, was accused of charging discount on notes payable at its own counter, and at the date of

^a Second Report of Bank Commissioners, Mass., 1840, pp. 15-16.

^b Fourth Report of Bank Commissioners, Mass., 1854, p. 83.

^c *Ibid.*, p. 84.

^d Tenth Report of Bank Commissioners, Mass., 1860, p. 136.

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examination this practice applied to about one-third of the notes under discount. This was in direct violation of the law. The excuse given by the officers of the bank was that exchange was only charged upon renewal of notes as a sort of penalty for having to continue the loan.^a

Rhode Island banks almost without exception secured extra interest through charging for exchange. * Rates of exchange on drafts were nominally one-fourth of 1 per cent on Boston and New York, rising to 2 per cent on the West and South. The banks charged from 1 to 2 per cent on four months' acceptances on New York in addition to the rate of interest. The total rate of interest therefore varied from 9 to 12 per cent. In 1836 the price of drafts was fixed by law, and exchange above one-fourth of 1 per cent for New England and New York, increasing to 2 per cent for points south of South Carolina and west of Ohio, was prohibited.

Bank commissioners of Maine in 1837 reported that there was no uniform rate of exchange on domestic bills. In Portland some of the banks took one-fourth of 1 per cent without regard to time, and others charged one-eighth, one-fourth, and even one-half per cent per month, making the amount of exchange dependent upon the time of the bill. This was obviously a method of obtaining unlawful interest. Similar criticism was made in 1857; each bank put its own construction on the term, "existing rate of exchange," which was authorized by law. Bank commissioners of Vermont in 1854 reported that most of the banks made a greater profit in selling drafts than that derived from their ordinary business; there was thus a

^a Twelfth Report of Bank Commissioners, Mass., 1862, p. 159.

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temptation to make it a condition of discount that the borrower should purchase a draft at a premium although he might not wish to use the funds in market.

Bank commissioners of New York in 1837 declared that the rates of exchange might be cut in half and there would still be a fair compensation to the banks. They did not, however, think that the banks had as much influence in regulating exchange as was generally supposed.^a

The governor of Mississippi in 1838 noted with disapproval that the banks of his State had devoted most of their funds to the purchase of bills of exchange drawn on cotton dealers, and condemned them for seeking to gain usurious interest in the shape of exchange, instead of discounting ordinary bills. In Georgia a legislative committee, in 1840, condemned the prevailing practice of dealings in fictitious bills as a substitute for promissory notes. In Alabama, the management of the Bank of the State of Alabama in 1837 voted that in order to relieve the existing commercial distress it would purchase six months' bills drawn against the shipment of the cotton crop of that year. The bank commissioners, however, complained of the growth of this business, for when the State determined to engage in the business of banking its primary object was to furnish a sound circulating medium and "to facilitate by small temporary loans the various branches of industry and laudable enterprise in which the citizens might engage;" dealing in bills of exchange was advantageous, but liable to great abuse, because adventurers could palm off upon directors bills not founded upon shipments, but rather those that were drawn purely for the accommodation of parties, known

^a Report of the Bank Commissioners, New York, 1839; see also Assembly Document No. 229, 1835, 3:4.

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as "kite bills," and the bank was accused of having taken a good deal of this paper. In 1840, however, the commissioners admitted that the banking system was not adapted to the requirements of a commercial community, for the State had changed from being a purely farming State to engaging in large operations in the sale of cotton. As illustrating the suspicion with which exchange business was regarded, the statement of the president of the Bank of the State of Alabama, explaining in 1840 why bills were not then purchased, may be cited: The charter and the legislature required for the purchase of foreign bills the action of at least three of the directors; but it was impracticable for such a committee to go into the exchange market and make the necessary purchases. There was also a restriction in the charter that all bills should have at least two good indorsers, and this form of foreign exchange could rarely be had.^a

In Ohio the bank commissioners in 1839 criticised the banks for refusing to discount domestic paper and giving preference to fictitious bills of exchange, in order to extract from needy borrowers a usurious rate of interest. Objection was also made to the high rates charged on legitimate bills; since the completion of the Pennsylvania canal, the cost of transportation from the Ohio River did not warrant a rate of over one-half to 1 per cent, but banks charged as high as 5 per cent. Some reform was made, for in 1844 it was reported that the majority of the loans during the previous year had been made on bills payable in eastern cities, founded on actual transactions. In 1850 rates on bills drawn out of the State were regulated by statute.

^aH. R. Doc., No. 111, 26 Cong., 2d sess., 522.

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In 1838 the state banking officials of Indiana complained of dealings in fictitious bills; there was no reason for banks undertaking to make remittances to other States, since banks were not created for the purpose of regulating domestic exchange. On the other hand, the State Bank, 1839, advised that some of its branches turn from loans on accommodation paper to exchange in order to carry off the produce; preference should be given to shippers of produce on exchange not having over six or seven months to run. This policy was definitely followed after 1844. A comparison of the dealings in promissory notes and bills of exchange by the State Bank, 1835 to 1858, is shown in the following table:

[From Harding, *Journal of Political Economy*, December, 1895, p. 114.]

Year.	Promissory notes.	Bills of exchange.
1835.....	\$1,500,000	\$400,000
1836.....	2,300,000	900,000
1837.....	2,900,000	400,000
1838.....	3,000,000	600,000
1839.....		
1840.....	2,600,000	800,000
1841.....	2,500,000	900,000
1842.....	2,200,000	400,000
1843.....	1,700,000	400,000
1844.....	1,700,000	500,000
1845.....	1,900,000	1,200,000
1846.....	1,700,000	1,400,000
1847.....	1,600,000	1,500,000
1848.....	1,700,000	1,800,000
1849.....	1,700,000	2,000,000
1850.....	1,800,000	2,500,000
1851.....	1,600,000	2,900,000
1852.....	1,500,000	2,800,000
1853.....	1,600,000	3,500,000
1854.....	900,000	3,400,000
1855.....	1,000,000	3,700,000
1856.....	900,000	3,900,000
1857.....	500,000	300,000
1858.....	200,000	200,000

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In 1855 it was made a misdemeanor for a stockholder, officer, or employee of a bank to purchase a bill of exchange of any Indiana bank for a less rate than that specified on the face of the bill.^a

In Kentucky the practice of making fictitious bills of exchange early received legislative attention; in 1817 the charter of the Bank of Kentucky was amended so as to prohibit dealings in bills "founded on a speculative system of acceptance." The handling of legitimate exchange business in Kentucky and Tennessee, however, became a serious problem. The products of these States, flour, mules, hogs, horses, rope, and bagging, were largely sent South, either to New Orleans or Charleston. It became the custom of the banks to reimburse themselves for the acceptances which they made by selling drafts on the East in payment of eastern merchandise purchased by merchants at home. This it was possible to do through the sale of the funds which accumulated to their credit. In detail, the business may be illustrated as follows: A farmer or manufacturer in Kentucky drew on a shipping merchant at Louisville; he cashed the bill at one of the branches of the Bank of Kentucky in the interior. This bill was then remitted to Louisville for collection and was there paid in drafts upon the East. Upon the credits thus accumulated the bank checked in favor of the debtor merchant in Kentucky who imported from that section. The banks were in the habit of charging something more for bills payable in the South than they had to give for eastern funds, and of charging a premium on eastern funds

^a Laws, Ind., 1855, ch. 7, sec. 41.

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when they sold them to the merchants. When the Bank of the United States ceased to do business in 1836, the rates were increased. The local banks explained this on the ground that arrangements could not be made with collecting banks in the South to furnish drafts at any definite rate or at any fixed time after collection. The latter would agree to furnish drafts only as eastern and northern funds could be procured. For this reason a charge of 5 per cent in addition to interest was justified, and even then it was maintained that profits were uncertain.^a

Trade was thus heavily burdened. During the earlier existence of the United States Bank bills of Kentucky traders in New Orleans sold at from 1 to 1½ per cent discount, and banks were accustomed to supply remittances in great abundance to any part of the United States at a premium of one-half of 1 per cent.^b

Banks, however, claimed that they did not demand extortionate rates; for the rate of discount charged upon bills drawn on points against which there was a balance of trade, was less than that charged by private brokers. It was admitted that the Bank of the United States had dealt upon better terms, but that was due to its national character. A local bank sometimes had to let its notes lie idle. For example, when the Northern Bank of Kentucky bought a bill upon New Orleans, payable at a season of the year when exchange upon Philadelphia or New York could not be procured, the funds of the Kentucky

^a Report of the Richmond Branch of the Northern Bank of Kentucky, 1837.

^b Message of the Governor of Kentucky, 1840.

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bank so invested lay idle in New Orleans as a dead deposit in a bank which paid no interest. The Kentucky bank, consequently, must of necessity compensate itself for this loss by charging a higher rate in New Orleans. The Bank of the United States did not have to undertake any such risk, for it could actively employ its funds through its branch at New Orleans.^a

Aside from these considerations, banks in the Southwest intentionally endeavored to increase their exchange business at the expense of ordinary discounting; for an advantage was found in the purchase of bills, because of greater certainty that they would be paid at maturity. Payment of a bill of exchange was thrown to a distant point and aid was thus given by banks other than that to which the bills belonged or at which they originated, while in the payment of ordinary notes custom had come to require whatever indulgence the bank could give.^b For quick assets, therefore, bills were preferred; for example, after the Northern Bank of Kentucky had been made a United States depository on condition that these deposits might be called for on demand, it invested them in short bills.^c

On the whole, such investments in Kentucky were regarded with approval. In 1837 a joint legislative committee of Kentucky argued in favor of bills of exchange; the bill business was limited by the actual operations of commerce; the accommodation business was as limitless as the want of money, rage of speculation, or the spirit of

^a Report of the Bank Commissioners, Kentucky, 1840.

^b *Ibid.*, 1839.

^c Northern Bank of Kentucky, 1837.

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gambling. In discounting a note a bank exchanged its own credit for that of the individual and received 6 per cent per annum for the difference; in purchasing a real bill, the bank bought a certificate of real value. A legislative committee in 1838 thought that the proportion of bills of exchange to notes under discount was too small; in the regular course of business the amount employed in exchange should be about one-third of all the investments of the bank, for without this proportion a sufficient amount of eastern funds to meet the demand for remittances could not be furnished. On the other hand, it was stated that, as a general principle, the banks ought not to be forced into the bill line, and any constraint to extend bills and diminish discounts would be an infraction of the charter and a violation of public duty.^a In 1840 a legislative committee gave its unqualified assent to the efforts of banks to convert their business paper into bills of exchange, although they admitted there was danger of going too far.

The Maysville branch of the Bank of Kentucky, 1840, in explaining why it had not invested as largely in bills of exchange as the mother bank desired, urged that this investment was seductive in its character because it introduced the evils of a fluctuating amount of circulation, expanding during the bill season and contracting during the year. The accommodation line had to approximate the amount of capital, and bills of exchange beyond accommodating the exporting and importing interest ought not to be encouraged. Later, in 1849, a legislative committee of Kentucky reported that, although the banks

^a Reports of the Bank Commissioners, Kentucky, 1838, 1839.

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could deal in bills of exchange, it deprecated the increasing tendency of banks to concentrate their capital in operations of this character. One of the first objects for which banks were created was defeated, for local accommodation was denied.

The charter of the Bank of Tennessee provided that the amount of bills of exchange for the parent bank or any one of its branches should not exceed the amount of notes discounted. The bank management, however, stated that some of the branches were located in districts in which bills could not be purchased. As it was believed necessary that the investment in such bills should equal the charter limits, it was suggested that permission be given so that the bank as a whole could hold an amount of bills equal to the notes discounted by all.^a In 1845 the president of this bank again referred to the desirability of exchange investments; hitherto this policy had not been sufficiently pursued; discounts by some of the branches had been made chiefly on accommodation notes, and on this kind of paper debtors were unprepared, either from habit or inability, to pay even moderate calls. The same advice was repeated in 1849, and it was then remarked that some of the branches had been benefited by the larger investment in this direction.

An illustration of the use of fictitious bills of exchange as a means of extorting usurious interest is to be found in a report of a legislative committee in Missouri in 1838, which helps to explain the prejudice against an operation which might be wholly beneficial. A person puts his note

^a Bank of Tennessee, 1839.

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into a bank, say for \$10,000; the bank tells him that the indorsers are good, but that they have not the money to loan. If he has a trade on hand of importance, he concludes to draw a bill of exchange on some person in a distant city who will accept and agree to pay it when due, four months thereafter. He draws his bill, gets two or three to indorse it, and then the bank, which before had no money, takes the bill and pays him the money, deducting a premium, say 5 per cent and the interest also. The premium is \$500, the bank interest is \$233.33; total \$733.33 for the use of \$10,000 for four months. At the end of four months, he makes another bill in the same way and sends the money to the city upon which he drew to pay the first one, when it becomes due; 15 per cent will thus be paid for premiums and 7 per cent for interest in the year. Add 5 per cent every four months for expense of transmitting the money to meet the bills, and the borrower pays 37 per cent for the use of \$10,000.

Over a large section of the Southwest exchange business after 1840 fell mostly into the hands of private bankers. Alabama, Mississippi, Florida, Illinois, Arkansas, and Michigan, with the Territories of Wisconsin and Iowa, had few banks, although a short time previous there had been a nominal capital of \$43,000,000 employed in the banking business. The results were satisfactory, for rates were lower and more regular than when charter banks abounded. According to a writer in the *Merchants' Magazine* in 1843, "private houses have a great advantage over corporations in the economy, precision, and skill with which the business is conducted. They contain also within themselves

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a conservative principle which constantly counteracts a tendency to overtrading. The facilities they offer for the collection of debts actually due is greater than that of banks; but, on the other hand, they afford no means to the debtor to evade payment or renew an obligation. Hence, when bills are due against any section for goods purchased the whole amount must actually be paid. By a necessary consequence the dealer, aware that the only means in his power to meet this obligation is by making cash sales to a corresponding amount, becomes very careful not to buy more than he thinks he can sell. When, therefore, a draft is made upon him, he has the means of meeting it; and as his sales have been governed by the actual means of the producers to buy, the means of remittance is always commensurate to the sum of the drafts. The bills of the produce shipper always find ready sale with the holder of the draft upon the dealer. Every mail from the seaboard which brings to the western house drafts for collection carries back produce bills in liquidation of those drafts."^a Again, in 1850, another writer compared the existing system of "free trade in exchange" with the old plan of monopoly under the United States Bank. Rates of exchange in New York were compared as follows: ^b

	April, 1833.	April, 1850.
New Orleans	1 to 1½ per cent discount . . .	Par to ½ discount.
Charleston	2 per cent discount	¾ per cent discount.
Savannah	do.	½ per cent discount.
North Carolina	2½ per cent discount	1½ per cent discount.
Richmond	1 per cent discount	¾ per cent discount.

^a Merchant's Magazine, 8: 563.

^b Ibid., 22: 551.

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(c) Length of loans.

During the earlier years of banking borrowers were apt to regard a bank as a benevolent rather than a money making institution, and as it possessed special grants by legislative favor it was held bound to accommodate the public. A bank was therefore criticised when it demanded that notes be paid at maturity, and that no renewals be allowed.

In Rhode Island the Providence Bank, the first established in that State, adopted a thirty-day limit on discounts, but the nature of its business forced renewals—a large part of the loans were made to aid the commercial interest and as the vessels took long voyages before settlements could be made it was necessary to secure long credits. The discounts of merchants approached very closely to long-time accommodation paper.^a The largest proportion of notes discounted ran for sixty days and of drafts and bills for four months. A legislative committee in 1826 reported that advances ought to be made by banks at long-time, as merchandise was sold on credit from four to six months. In 1857 it was customary to make loans to the textile manufacturers on long credit—eight, ten, and twelve months' discounts were common, while those under four months were rare. After the panic of 1857 a six months period for credits was for a time observed.^b

In Connecticut, by the rules of the Hartford Bank, 1792, loans were not to exceed forty-five days. This term was quickly extended to sixty days, and in 1809, to three

^a Stokes, *History of Chartered Banking in Rhode Island*, p. 14.

^b *Ibid.*, p. 51.

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months. This became the usual rule.^a The rules of the Worcester Bank, Massachusetts, 1804, limited discounts to sixty days; all loans on lands and mortgages were to be made for one year.

The Bank of New York, 1784, began with a maximum period of thirty days and permitted no renewal.^b Very shortly the time was extended to forty-five days,^c and then loans for longer periods became common. Eight months was an established period for New York importers, and Boston banks afterwards claimed that they were forced to submit to the same length of time for manufacturers. In 1857 there was an interesting exchange of opinion between a New York banker, Mr. John A. Stevens, and Mr. Nathan Appleton, of Boston. The former criticised the banks for the granting of long credits. In reply Mr. Appleton stated that while he was opposed to long loans, he did not think that banks should confine their discounts to short paper which, even if good for banks, was bad for the community. "I have been for upward of forty years a director of a Boston bank, during the greater part of which time they have confined their discounts to real business paper which should be paid at maturity and have not refused it even when having six months to run. This system has worked well and always gives the bank enough coming in to meet any emergency. I hardly recollect a discount day when the bank has not been able to discount some new paper."^d

^a Message of Governor Wolcott, May, 1822.

^b Domett, Bank of New York, p. 20.

^c *Ibid.*, 38.

^d Bankers' Magazine, 12:407.

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The Bank of Pennsylvania restricted its loans to sixty days, and the Philadelphia Bank, 1804, to four months. According to Raguet, in the first part of the century it was not a general practice in Philadelphia to discount notes that had more than sixty days to run. Within thirty years, owing to the competition of banks and the increase of bank capital for which short paper could not be found, it became the custom to discount four and six months' paper. To this extension is attributed in part the gravity of the suspension of 1837.^a

In Maryland the banks differed as to the length of their discounts. Country banks as a rule gave longer periods than city institutions. After 1808 this point was generally regulated by charter; in those granted between 1810 and 1818 two banks were limited to sixty days, one to four months, nine to six months, and for two there was no limit.^b The Mechanics' Bank discounted notes up to four months, and on a loan secured by property the maximum time was two years.^c

Virginia, in the charter of the Bank of Northwestern Virginia, 1817, adopted one hundred and twenty days;^d and later it made for all banks six months as the maximum limit.^e In South Carolina the Bank of the State, 1812, was forbidden by its charter to loan for more than a year.

^a Financial Register, 1838, p. 9; see also Raguet, *Currency and Banking*, p. 96.

^b Bryan, *State Banking in Maryland*, p. 71.

^c Maryland Laws, 1806, ch. 19.

^d Laws of Virginia, 1817, ch. 39, sec. 11.

^e Charter of the Merchants and Mechanics' Bank, 1834; general law of 1837.

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Alabama, in 1839 and 1840, passed acts for the relief of debtors. In 1839, for example, it was provided that not exceeding 20 per cent of the debt due a bank on notes running to maturity or upon bills and notes in suit, or upon which judgments had been obtained, could be collected in any one year. The Bank of the State of Alabama at Huntsville consequently required notes to be given for one hundred and twenty days. This legislation led to an increase in the suspended debt and put the banks in a worse position than they were before. The commissioners which examined the branch of the Bank of the State of Alabama at Decatur in 1840, however, thought that such legislation was highly desirable and commended the action of the management of the bank, which, "actuated by motives of benevolence and philanthropy, had withheld a large amount on which suits might have been commenced. A policy nicely discriminating between the claims of those having the means and neglecting to pay their installments, and those who, without distress to their families, cannot raise the means to do so, is, in the opinion of the board, the true policy."^a

(d) Renewals of loans.

The Bank of Hartford, 1792, prescribed that any person not punctual in meeting his note was not to receive further loans. In 1809 it was ordered that a payment of 20 per cent would be expected on a ninety-day loan at maturity, and that no renewal would be received for a greater sum than four-fifths of the principal falling due.^b In 1821 the

^a H. R. Document, No. 111, 26th Cong., 2d sess., p. 612.

^b Woodward, *The Hartford Bank*, p. 88.

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management voted that notes which had been put in the hands of an attorney for collection should not be renewed. The Worcester Bank in Massachusetts ordered that no notes should be renewed for more than four-fifths of the original sum and at every renewal one-fifth of the original loan should be paid in.^a

By the rules of the Bank of New York, 1784, renewals of loans were not permitted. The by-laws of the Girard Bank, of Philadelphia, 1832, forbade the renewal of a note for a sum equal to that originally discounted, and justified renewals only in case of mistake, accident, or urgent necessity, to be determined by the sound discretion and judgment of the president.

In South Carolina the Bank of the State, 1812, forbade renewal unless a year's interest was paid in advance. One-tenth of the loan was to be called in each year. The Central Bank of Georgia, 1828, renewed accommodation notes every six months. The Planters' Bank in Mississippi, 1830, could not renew real estate loans until one-fourth of the principal was paid. By an amendment to its charter in 1833 loans could be renewed for one, two, or more years at a 9 per cent interest. The Union Bank of Louisiana, 1832, a real estate bank, gave renewals at the end of a year, provided one-eighth was paid, thus allowing a loan of eight years.

By the middle of the century renewals and extensions were the exception rather than the rule.^b

^a Worcester Bank, 1804-1904, pp. 8-9.

^b Merchants' Mag., 22:89; 17:511.

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(e) Amount of loan to any one person.

In accordance with the idea that banks should distribute their benefits as widely as possible, limitations in some States were placed upon the amount which could be loaned to any one person. Such restrictions do not, however, appear in the early charters of New England. In the course of time bank commissioners began to complain of the excessive amounts granted to single individuals, and in 1838 the commissioners of Connecticut recommended that individual discounts be restricted to a certain percentage of the capital. The legislature, however, took no action, and in succeeding reports similar complaints were made. In 1847 it was reported that banks with less than \$100,000 allowed single discounts amounting to \$30,000. In 1854 a bank with a capital of \$80,000 had loaned nearly \$50,000 in one case and \$42,000 in another. In that year the legislature took action and passed a law providing that no loan should be made to any person or corporation for more than 15 per cent of the capital. There was still dispute, for some of the banks construed this liability as applicable only to a direct loan.^a In Vermont, by an act of 1840, no individual could borrow more than 10 per cent of the capital. As the result of a special inquiry in Rhode Island in 1843 it was found that one bank had loaned \$72,000 to one borrower, and that another bank, organized in the interest of farmers, had made a single loan of over \$25,000.

The Bank of New York about 1810 reduced the maximum of a single loan to any one person to \$20,000, but the

^a Acts, Conn., ch. 11, sec. 2.

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legislature of that State did not impose restrictions. The Bank of Pennsylvania limited the total indebtedness of any individual or firm to \$50,000.

In Maryland, by the charter of the Mechanics' Bank, 1806, loans on property, which could be made only to one-eighth of the paid-in capital, were limited to not more than \$3,000 to any one person.^a Virginia required of her banks returns in regard to the amount of individual discounts. In 1837, for example, the Merchants and Mechanics' Bank of Wheeling reported these loans:

Over \$20,000.....	1
\$10,000 to \$20,000.....	20
\$5,000 to \$10,000.....	163
\$1,000 to \$5,000.....	1,357
\$500 to \$1,000.....	1,065
\$200 to \$500.....	1,634
\$100 to \$200.....	1,133
Under \$100.....	626
Total.....	5,999

The charter of the Bank of Kanawha (Va.), 1839, made elaborate provision by which small loans were to take precedence over large ones. Applications for discounts were divided into five classes, as follows: (1) Applications for sums \$100 to \$500; (2) applications for sums \$500 to \$2,000; (3) applications for sums \$2,000 to \$5,000; (4) applications for sums \$5,000 to \$10,000; (5) applications for sums \$10,000 to \$20,000. All applications in the lower classes were to be granted before giving an application in the higher classes. The total indebtedness of any one person or company was limited to \$50,000.^b

^a Maryland Laws, 1806, ch. 19.

^b Laws, Va., 1839, ch. 87, sec. 3; see also ch. 88, sec. 13.

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In South Carolina, the Bank of the State, 1812, could not make a loan larger than \$2,000, and loans on mortgages must be apportioned between the election districts. Georgia in the Central Bank, 1828, limited its loans to \$2,500 to any one person and they were required to be distributed as equally as possible among the citizens of the State, according to population. In 1840 the bank reported that in accordance with the recent act of the legislature it had just completed the distribution of \$750,000 to citizens of the counties.

By the charter of the Bank of Alabama, 1823, it was provided that loans should be apportioned among the counties of the State in proportion to their representation in the general assembly, and the counties were to be notified of the amounts their citizens were entitled to borrow; in 1837 the Branch Bank of the State of Alabama was criticised because it did not wait for the elections in order to determine the proper apportionment of loans in different parts of the State.^a

The Planters' Bank of Mississippi, 1830, was limited to \$4,000 on any one real estate loan. The Mississippi Union Bank, which began operations in 1838 by resolution of its board of directors distributed its loans on personal security as equally as applications would admit, to the citizens of the whole State; \$2,855,000 were thus loaned during the first four months; the largest amount loaned to any one person was \$10,000, and this in only two cases; the average of the loans was \$1,800. In 1840 an act was passed requiring that no loans be made for more than

^a See 25 Cong., 2 sess., H. R. Doc., No. 79, p. 536.

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\$20,000 to the principal and for not more than \$50,000 to an endorser.

The Bank of Kentucky, 1834, could employ only two-fifths of its capital in Louisville, the remainder being reserved for the scattered branches.^a In 1843 the banks of Kentucky were required by law to loan to citizens in each of the Congressional districts where branches of the Bank of Louisville were not located, upon new accommodations.^b

Kentucky in its bank returns demanded a classification of loans according to the amounts demanded from each bank. Returns of the Northern Bank of Kentucky in Lexington, 1837, classified borrowers as follows:^c

\$100 to \$500.....	251
\$500 to \$1,000.....	155
\$1,000 to \$5,000.....	205
\$5,000 to \$10,000.....	33
\$10,000 to \$20,000.....	7
Above \$20,000.....	3

In 1839 the banks reported that they endeavored to distribute their accommodations as widely as possible. One of the larger banks, for example, stated that "in making loans we have endeavored to disseminate large accommodations in proportion to demand. It has been the studied effort of this bank to equalize bank accommodation and facilities among the surrounding and neighboring counties."

^a Duke, History of Bank of Kentucky, p. 38.

^b Act of March 8, 1843, sec. 15. Duke, History of Bank of Kentucky, pp. 98-99.

^c See Senate Document No. 471, 25 Cong., 2d sess.; also Document No. 172, H. R. 26th Cong., 1st sess., p. 749, *et seq.*, also p. 785.

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In Tennessee there was the same solicitude that loans should be distributed throughout the State. The Bank of Tennessee, 1839, at its organization, published a statement in the newspapers as to the amount which each county was entitled to borrow, the proportion being determined by population.^a

In Indiana, by the charter of the State Bank, 1834, no corporation could borrow more than 5,000 at any one branch, except by permission of the central board. In 1839 complaint was made of the great inequality in the grant of loans to citizens of the different parts of the State; less than one-twentieth of the people of the State enjoyed discount privileges; of the 5,000 borrowers, 600 were stockholders and directors who took more than a third of the total; three-fourths of the loans were devoted to thirteen of the counties, or less than one-sixth of the whole number; the farmers, who constituted about three-fourths of the people, received but one-fourth of the discounts; the merchants were the favored class, and the loans which they received were injurious, in that it made it possible for them to obtain large purchases abroad on credit and thus stimulated on the part of the people a love of indulgence and display which increased the consumption beyond the production. Illinois, in 1840 (Jan. 3), restricted single direct loans by the State Bank to \$10,000 and indorsement to \$25,000.

^a See Report to the Legislature, Oct. 7, 1839.

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(f) Loans to directors.

During the second period of banking, when banks were organized more for the personal profit of the stockholders than to serve public interest, the question of loans to directors engaged much attention. In Massachusetts an act was passed in 1838 limiting the amount for which directors and officers might be liable unless the stockholders by an express vote authorized a larger sum. This was perhaps due to an investigation of the Commonwealth Bank, in which it was found that excessive overdrafts had been allowed to directors; although the management had voted some ten years before that no money should be drawn from the bank by memorandum check or overdraft, the practice continued and it was claimed that there were similar practices in other banks. This informal method of borrowing was largely in favor of directors.^a In 1838 and again in 1851 limitations were imposed restricting an individual director to 8 per cent and the whole board to 30 per cent of the capital except by express vote of the stockholders;^b in 1843 the cashier and subordinate officers were forbidden to borrow of the bank.

In Connecticut in 1819 the Hartford Bank, following a policy of increased caution, voted that any director offering a note for discount should absent himself from the board meeting while the loan was under consideration;^c and in 1839 it forbade loans to its president.^d The bank

^a Report of the Bank Commissioners, Mass., 1838.

^b First Report of Bank Commissioners, Mass., 1851, pp. 7-9; Second Report, 1852, p. 11.

^c Woodward, *The Hartford Bank*, pp. 125-126.

^d *Ibid.*, 147.

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commissioners of this State as early as 1837 called attention to the impropriety of large loans to directors. These were lenders to the bank and there was a strong objection to their being also borrowers. As a result, in the following year an act was passed disqualifying a person to serve as a director whose indebtedness to his bank exceeded \$9,000 above the stock in his name, and in 1840 it was further enacted that the directors collectively should not be indebted for more than one-third of the paid-in capital. Notwithstanding this restriction commissioners found reason for continued criticism. In 1841 the direct loans in fifteen banks to directors amounted to \$311,000 on a total capital of \$2,438,000. In some banks the directors were indebted to nearly one-third of the capital on accommodation paper only, and if their indirect liabilities as indorsers were taken into account the indebtedness would amount to one and a half. A more restrictive law was consequently passed, but there were complaints that the services of some valuable men were lost to banks of small capital. There was additional embarrassment because the law prohibited a loan to any company or corporation of which a director was a member or stockholder.

In Vermont, by the safety fund act of 1831, directors as well as stockholders were limited in loans to \$2,000, but this provision was easily evaded. In 1840 it was enacted that no stockholder or director should be indebted for more than 5 per cent of the capital, and that all of the directors together should not be indebted to a greater amount than the aggregate amount of 3 per cent for each director. In 1854 the bank commissioners reported

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that, in spite of legal restrictions, there was no limit to the indebtedness of any one; it was possible to evade the law because indebtedness arising from the purchase of bills of exchange was excepted in the percentage calculation.

In Maine directors' loans were restricted to 8 per cent of the capital, but the bank commissioners in 1842 reported that some directors borrowed more than the law permitted and declared that this abuse was responsible for more failures of banks than any other one cause. The practice became an abuse in Rhode Island, and in 1837 it was reported that banks, to a considerable extent, were simply engines to supply directors with money. At two of the banks one-half the discounts and at another three-fifths were for the accommodation of directors and firms of which they were members.^a

New York, in 1811, regulated the amount which a director could owe to a bank,^b and under the safety-fund act of 1829, directors were restricted from receiving discounts, including indirect liabilities, for more than one-third of the capital; in 1842 the bank commissioners declared that they thought it was unwise to restrict loans to directors too rigidly; these officers were generally men who were active in business in the vicinity of the bank and presumably would be able to meet their engagements.^c

In New Jersey the by-laws of the Newark Banking and Insurance Company, 1808, limited the liabilities of directors according to their property. A separate loan to any

^a Report of Bank Commissioners, Rhode Island, 1837.

^b Session Laws, N. Y., 1811, ch. 64.

^c Report of Bank Commissioners, New York, 1842.

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one person or firm was limited to \$15,000 and the maximum total to \$30,000. Loans to directors were arranged in three classes, according to their property: To those with the "best estates," \$12,000 was granted; to the second class, \$8,000; and to the third class, \$5,000. It was left to the "good judgment" of each director to classify himself, and the bank adopted the resolution "to earnestly recommend to every director of this bank to abstain from drawing, accepting, or indorsing for the accommodation of any person or persons whatsoever, except for such amounts only as their circumstances and resources would enable them to pay in case of their friends' failure."^a By a charter in 1824 no director could borrow more than the value of his bank stock;^b and beginning with 1830 charters frequently forbade loans to stockholders or directors or on notes drawn by one director and indorsed by another.

By the charter of the Mechanics' Bank of Maryland the president and directors could not borrow on accommodation paper more than \$9,000. In 1818 it was provided that the officers of the bank should have the same loaning privileges as officers of any other bank in the State;^c and in 1820 it was provided that directors should be entitled to discounts on the same terms as any other person.^d There was considerable legislation in regard to the amounts which directors could receive; in the charter of the Farmers' Bank at Annapolis, 1804, directors were prohibited

^a Charles J. Rockwood, *One Hundred Years, a Record of the Work of the Oldest Bank of the State of New Jersey*, pp. 12-13.

^b Acts, N. J., 49 Ass., p. 111, sec. 13.

^c Session Laws, Md., 1817, ch. 39.

^d Session Laws, Md., 1819, ch. 134.

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from receiving discounts on different terms from others.^a Afterwards a definite limit was placed to the amount of discounts which directors might receive: For the Farmers' Bank the limit was \$1,000 a week, for the Mechanics' Bank of Baltimore the total was fixed at \$9,000 renewable at discretion, and for the Hagerstown Bank \$500 a week.^b Whenever discounts to directors on accommodation paper exceeded \$9,000 the directors were to be informed and discounts to such persons were to be curtailed at the discretion of the board. In 1837 a legislative committee reporting on this subject stated that such discounts were reasonable and proper inasmuch as they were made to merchants and manufacturers who were responsible.

The general banking law of Virginia, 1837, forbade a director who was interested in a loan to be present when the application was considered, and in 1842 a law was passed limiting a director or firm of which he was a member to an indebtedness of not more than \$5,000.^c The charter of the Bank of Alabama, 1823, forbade bank officials to indorse for one another. In 1836 (Dec. 17) an act was passed making it unlawful for a director to be liable for more than \$35,000. Loans to directors, however, became an abuse, and in 1837 the bank commissioners reported them as excessive. It was stated that presidents and directors were indebted for over \$1,000,000 and ex-presidents for more than double that sum.^d In 1839 the legislature prohibited directors from becoming liable in any manner.^e

^a Laws, Md., 1804, ch. 61.

^b Bryan, *State Banking in Maryland*, p. 36.

^c Laws, Va., 1841-42, ch. 105.

^d Report of Bank Commissioners, Ala., 1837.

^e Acts, Ala., Jan. 13, 1839.

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Directors in the Planters' Bank, Mississippi, 1830, could not legally borrow more than \$6,000 at any one time, and in 1840 (Jan. 21) loans of any amount to directors were forbidden to all banks.

Clibborn, an Englishman, after five years' residence in Cincinnati, wrote in 1837, as the result of his observation, that banks would not discount unless the directors were directly or indirectly interested. A more serious abuse was the practice by directors of indorsing for a consideration of 1, 2, or more per cent. The bank commissioners of Ohio, in 1839, criticised the excessive loans which had been made to directors and officers where the direct liabilities amounted to a sum nearly equal to all the specie of all the banks. In Indiana the charter of the State Bank of Indiana, 1817, limited loans to a director to \$5,000 and his indorsements to \$10,000, but this restriction does not seem to have been sufficient. In a report made November, 1840, it was stated that discounts to directors amounted to about one-ninth of the total loans and the discounts to other stockholders to about one-fourth. In 1855 it was enacted that no director could be indebted for more than double the amount of his shares in the bank, except on bona fide bills of exchange, payable out of the State.^a In Kentucky a legislative committee, in 1837, investigated loans to directors and found that as payers on discounts and as drawers of bills the total amount to 31 directors in three banks was \$1,224,000. This, however, was less than loans to the same number of persons not connected with the management.

^a Laws, Ind., 1855, ch. 7, sec. 37.

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(g) Partiality in making loans.

Allied to the practice of making excessive loans to directors was partiality in the granting of discounts. In Connecticut there was for many years complaint that banks were partial to directors and their friends. In 1839 the bank commissioners stated that directors' loans were long-continued and renewed, thus tying up funds to the disappointment of men in active business. On the other hand, the Worcester Bank in Massachusetts in its petition for a renewal of charter in 1811 gave as one of the reasons for favorable consideration, that loans had been made without partiality and stockholders had been among the smallest borrowers.

In 1806 the Bank of North America in Philadelphia was subject to an investigation from which it was learned that directors had been in the habit of granting loans almost exclusively to a few favored individuals.^a During the embargo period, when money pressure became great, the banks denied the applications of those forced to turn to money lenders or brokers who in many cases were agents of bank directors and who, because of their official relations, were able to control the loanable funds of banks to their own advantage.

The historian of state banking in Maryland also notes that there was considerable dissatisfaction because discounts were confined to a small number of friends of banks and were not made on the merit of paper offered.^b

^a Lewis, *The Bank of North America*, p. 84.

^b Bryan, *State Banking in Maryland*, pp. 36-37.

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The branches of the Bank of the State of Alabama had a by-law by which each director on discount day could call up out of the regular order two notes and have them discounted as a matter of right in order to meet the needs of special cases. This practice easily degenerated into favoritism, and in 1838 the bank examiners reported that much of the apparent dissatisfaction with the State Bank and its branches had grown out of the partial manner in which discounts had been made and the large amount of discounts which had been granted by directors to themselves. It was estimated that the legal voters in the State numbered 55,000. Of these only 11,611 were indebted to the banks. The president and directors had borrowed over \$1,000,000 and ex-directors more than \$2,000,000, while others had obtained direct accommodations to the amount of \$3,054,000.^a By an act of February 2, 1839, provision was made for compensation to directors, in the hope that by payment for services their readiness to recompense themselves at the expense of the bank would not be so great.

The governor of Mississippi, on January 17, 1838, in a message stated that the bank commissioners reported that a few persons had obtained control of banks and made most of the loans to commission merchants, speculators, and officers of the banks. The banks consequently were dependent upon the planters.

^a Report of Bank Commissioners, Ala., 1838.

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(h) Restrictions on loans to residents and nonresidents.

During the earlier period of banking loans were generally made to persons living in the vicinity of banks. Acquaintance or citizenship was regarded as a necessary requisite; for example, by the rules of the Hartford Bank, 1792, the drawer or indorser of a note must be a resident of Hartford.^a Beginning with about 1830 there was an excess of banking capital in some sections of New England, due to the desire of bank organizers and promoters to secure profits through circulation. In order to earn these dividends it was necessary to make loans outside of the immediate vicinity in which the bank was established. This was looked upon with disapproval by conservative financiers and generally criticised by the bank commissioners. For example, the bank commissioners of Massachusetts, 1841, reported that several banks were in operation which were not needed. They could not loan their funds upon good business paper in the vicinity, and loans, therefore, had to be made upon accommodation paper which had to be "traveled for." This was generally second-rate paper. Directors could not acquaint themselves with the character of business at a distance, and it was remarked that the best class of paper did not travel abroad to be discounted in strange places. Sureties upon such paper were inclined to take advantage of technicalities in order to avoid prompt payment.

During the years 1852-1855 this subject again excited public attention. In the former year the bank commissioners referred to loans which had been made by banks

^a Woodward, *The Hartford Bank*, p. 21.

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to parties in distant States which were not based upon business transactions, but rather with the view to extending circulation. It is noted that paper thus inconsiderately taken was frequently not paid at maturity, that renewals were submitted to, and that serious losses closed the operation. It was also reported that loans were made by Massachusetts banks with a small amount of local business to banks outside the State whose stocks were pledged to secure the redemption of their own issues and whose profits were derived from the higher rate of legal interest in other States.^a In 1853 a legislative committee, in reporting upon additional bank capital, stated that there were two rules which should be observed: first, that the business of any given locality needed the use of any capital asked for; second, that there was capital there, or in the neighborhood, seeking that form of investment. It was observed that there was a very considerable portion of the loans of some banks represented by names and collateral remote from home, frequently in the West; this use of a bank's resources operated harshly on those in the vicinity who looked for business accommodations to the banks. Some of these loans, apparently well secured, had been made on advances from railroad and other enterprises, which, however, were incomplete; as a consequence, they must be renewed, and however urgent might be the wants of the local neighborhood, they could not be called in. A bank commissioner admitted that an opinion had been expressed in some quarters that banks were not bound to regard the wants

^a Second Report of the Bank Commissioners, Mass., 1852, p. 8.

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of their neighbors or to be confined within the Commonwealth in dispensing discounts, thus making all public considerations give place to the interest of the stockholders. This doctrine, however, they were happy to say, was rarely advanced and one which it was hoped would never find favor with the public or the legislature.^a In the following year they called attention to the disastrous consequences of the policy previously reprehended; several banks which had indulged in remote loans had been forced to pass their dividends.^b In 1859 the commissioners again criticised the practice of forcing loans at a distance: The bank officer who loaded his carpet-bag with notes of his bank and wended his way to State street, there to conduct the business of the bank with brokers and sharpers, was doing an ill-advised business; it would be better if he devoted his efforts to extending the bank's circle of customers at home and thus create a safe and reliable circulation. It was, however, impossible to prevent the practice, for in 1860 it is again noted that there was a growing custom among the banks to seek paper for discounting among brokers.^c Notwithstanding these official cautions, the Boston Board of Trade, in 1857, memorialized the legislature to the effect that there was an insufficiency of banking capital, which caused merchants and manufacturers to resort to New York and elsewhere for the negotiation of a large part of their business paper.^d

^a Fourth Report of the Bank Commissioners, Mass., 1854, p. 82.

^b Fifth Report of the Bank Commissioners, Mass., 1855, p. 73.

^c Tenth Report of the Bank Commissioners, Mass., 1860, p. 137.

^d Bankers' Magazine, 1857, 11:902.

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In Connecticut, loaning abroad was regarded by the bank commissioners as a serious evil. Beginning with 1837 there is hardly an annual report in which the subject is not referred to. In 1837 it was reported that the legislature had never incorporated a bank except on the consideration that its capital should be employed in the neighborhood of its location. Banks ought not to loan in another State. It was noted, however, that some had lent large sums to strangers in remote parts of the United States, and that, in particular, the Middlesex County Bank had discounted paper in New York City and a considerable amount in Chicago. Complaint was made that the City Bank of New Haven had made large loans outside the State without due regard to the needs of New Haven; in 1836, for example, discounts amounting to \$401,000 were made in the State and \$1,337,000 outside the State. In the desire to secure large profits the bank had lost sight of public interest. The total proportion of loans to citizens in Connecticut and to those outside was one to eight; in 1831 it had been only one to five. In the next year it was stated that Connecticut banks kept funds, varying from \$1,000,000 to \$1,500,000, in New York in the hands of brokers of banks. This policy was open to criticism, because there was a need of capital at home and loans ought not to be placed beyond the jurisdiction of the State. In 1841 they reported that the greatest losses which banks had sustained were due to the large amount of loans without adequate security, in the hands of brokers, and also to loans made mostly in the western part of New York in 1837 and 1838. In 1844 it was admitted that

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banks found it impossible to find use for all their notes in discounting good paper at home, and consequently reduced their rates. Banks, however, had been tempted to make investments in stocks, and large balances accumulated in New York City, on one-half of which interest was allowed. This led to injurious consequences, for a large amount of unemployed capital in New York City had a tendency to advance the price of stocks and to develop a spirit of speculation. No longer did the banks enforce the sound and wholesome rule requiring at least one responsible indorser within the State.^a In 1854 they again complained of the placing of notes in the hands of brokers who were engaged in railroad enterprise and stock speculation. Seven banks had loaned to a New York broker, engaged in the construction of a western railroad, \$508,000. Banks had also purchased negotiable paper in large amounts in New York at rates of discount exceeding that permitted by the law at home. Thus they were obliged to curtail domestic accommodations. Finally, in 1855, ^b a law was passed prohibiting any Connecticut bank from loaning outside the State more than one-fourth of its capital actually paid in and deposits. In the next year it was reported that the loaning of money abroad on railroad securities had been to a great extent discontinued, but in 1857 reference was again made to the illegal practice of discounting paper abroad at rates ranging from 7 to 12 per cent, under the plea that paper bought on Wall Street was not discounted, but bought. A large amount was

^a Report of the Bank Commissioners, Connecticut, 1847.

^b Acts of Conn., 1855, ch. 11, sec. 5.

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annually sent to New York for investment in bonds and mortgages at 7 per cent, making it difficult for manufacturers and traders at home to get the necessary facilities at 6 per cent. In 1862 the commissioners reported that the law requiring the banks to loan to persons in the State an amount equal to their capital stock before they loaned outside had not been observed by many of the banks. These still loaned for accommodation or circulation in the West.

In 1836 the bank commissioners of Rhode Island noted with disfavor that the directors of the Newport Exchange Bank had made large purchases of paper in New York, as well as in Providence, and recommended that the practice of discounting abroad should be corrected by the legislature.

The bank commissioners of New Hampshire in 1840 reported that the Wolfboro Bank had made very large loans to individuals outside the city, particularly in New York and New Jersey; \$105,000 had been loaned to a single person in New York City, and apparently a very considerable part of this was without security beyond personal responsibility. In 1841 the bank commissioners recommended that banks be restricted from loaning to persons outside the State more than one-fourth or one-fifth of the capital.

By the charter of the Union Bank of Maryland, 1805, discounts upon personal security required the names of two responsible persons, residents in Baltimore; if other security was given only one name was required, but in that case property should be so conveyed that it could be sold

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immediately. The bank commissioners of Ohio referred with disapproval to the prevailing practice of banks in opening accounts with distant individuals or brokers. This disregarded the purpose of the bank charters; favors were intended for persons living in the immediate vicinity of the bank. The charter of the Bank of Kentucky, 1806, provided that loans could be made only to citizens of the State.

In closing this account of the investments of banks it should be noted that some banks followed the path of prudence, as judged by the most conservative standards of the present day. Such an institution was one in Connecticut, of which Mr. Isaac Bronson was president for more than thirty years during the earlier half of the century. He never discounted paper at his counter for a longer period than sixty or ninety days and would not in any instance consent to a renewal. Consequently after the bank had been a short time in operation the payments made on the discounted paper equaled the emissions of bank bills. Thus the means of redeeming all the paper he issued soon became ample, by the fruits of discounts only, without the employment of any capital. Every bill which remained in circulation was soon represented by its equivalent in specie in the vaults of the bank. During all this time he would be gradually investing on good security and on half yearly interest the specie capital of the bank so that two classes of customers would be accommodated—those who needed discounts for sixty or ninety days with bills advanced on indorsed notes at the counter, and those who wanted loans for months or years,

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with the specie capital, on giving safe security. The specie capital was all soon lent on half yearly interest, and the discounts could be indefinitely extended as they supplied the means for redeeming all the bills of the bank without resort to the capital. The revenues of the bank from these two sources made an average dividend of ten per cent yearly during the whole of Mr. Bronson's administration. This bank, without resort to its capital, although its discounts were liberal, was one of the few which sustained specie payments during the war of 1812.^a

XXIV. LOANS TO STATES.

There were two opposing principles which influenced legislation in regard to the making of loans by banks to state governments. On the one hand was the fear that governments might become too dependent upon banks; on the other, a growing conviction that the States ought to receive financial assistance from institutions which were chartered as grants of special favor. This conflict of opinion is well illustrated in the charter of the First United States Bank. As already stated, one of the reasons assigned in the preamble for incorporating this institution was to make loans to the Government in sudden emergencies, and yet it was carefully provided in Article xi that no loan should be made to the National Government for more than \$100,000, or to any particular State for more than \$50,000, unless previously authorized by Congress. In this way it was believed the financial relations of banks to state governments could be kept

^a Financial Register, 1838, 2:15-16.

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under control, but on the whole the desire to make the banks supporters of public credit was more powerful than the fear of their ascendancy. This is seen in the provision of the First and Second United States Banks which called for the subscription of a large part of the capital in government securities. Indirectly this was a loan of capital to the Government. Later it was recommended by able writers, as by Gallatin, that all of a bank's capital should be loaned to the Government, that is, invested in public stocks.^a Gilbert, an English authority, in contrasting American with English banking practice, criticised our policy of requiring banks to make loans to the Government, on the ground that the latter would require them only in times of distress when banks were least able to make them.^b

It was a common practice in many States to require banks to make loans, if called upon, to the State which chartered them. In Massachusetts, for example, the charter of the Union Bank, 1792, required it to loan the State a sum not exceeding \$100,000 at 5 per cent, and a similar provision was applied to most of the banks subsequently organized. By the charter of the State Bank in 1811, the State could borrow at any one time a sum not exceeding 10 per cent of the capital, payable within five years at 5 per cent, but the total liability to the bank was limited to 20 per cent of the capital. By an act of 1816, the treasurer of the State was authorized to enforce loans and was given power to levy a fine of 2 per cent a month on sums

^a See also Lord, *Principles of Currency and Banking*, 1829, pp. 72, 84.

^b Gilbert, *History of Banking in America*, p. 88.

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refused.^a In some cases loans to the State were so large that the banks were weakened for commercial purposes. Ten per cent of the capital became the common rule, until 1829, when the general law made 5 per cent the ratio for any one loan, and 10 per cent the maximum total. The penalty of 2 per cent per month for refusal was continued.

Though not compelled by its charter, the Bank of New York in 1794, at the request of Secretary Hamilton, made a large loan to the Federal Government and it also accommodated the State.^b The Mechanics' Bank of New York, 1810, was under obligation to loan one-sixth of its capital for three years at 5 per cent. In 1812, when the old Bank of the United States was reorganized in New York as the Bank of America, it had to pay a heavy price. The act of incorporation called not only for a loan of \$100,000 at 5 per cent and one of an equal amount at 6 per cent, but also demanded the payment of a bonus of \$400,000. These conditions proved so onerous that they were subsequently remitted.^c New Jersey, in 1815, required the Farmers' Bank to loan to the State \$50,000 on thirty days' notice.^d

Pennsylvania forced her banks to lend their credit as the price of organization. The Philadelphia Bank, 1804, was required to loan \$100,000 at not over 5 per cent for five years, in addition to a gratuity. In 1814, the law chartering a large number of new banks demanded that each should loan to the State one-tenth of the paid-in capi-

^a Acts, Mass., 1816, ch. 133, Jan. sess., p. 177.

^b Domett, Bank of New York, pp. 50, 54.

^c Acts, N. Y., March, 1813, and February 26, 1819.

^d Priv. Acts, N. J., 39 Ass., 1 sess., p. 162.

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tal for five years, and this requirement was repeated in the general banking act of 1824. In 1825 the Bank of North America, in securing a renewal of its charter, was called upon to loan one-twentieth of its capital at 5 per cent.^a In addition to charter requirements, special acts were frequently passed authorizing specific loans from banks. Between 1820 and 1830 the Bank of Pennsylvania, in particular, was called upon to render extensive aid, so great indeed that it involved the bank in serious embarrassment. In 1828 an attempt was made to incriminate the directors for making large loans to the State, while, on the other hand, in the next year the bank was publicly attacked for not loaning the amount desired by the State, and thus crippling certain plans of internal improvement.

In Maryland the legislature at the beginning of her banking policy was disposed to fear the results of a too great dependence of the State upon banks. The charter of the Bank of Baltimore, 1795, imitated by others, limited the amount of credit to the United States or to any State, including Maryland, to \$50,000.^b Between 1812 and 1816, doubtless moved by the exigencies of war, these restrictions were removed and all banks were permitted to loan to the State of Maryland up to the amount of capital and to the United States up to one-third of the capital.^c

North Carolina, by the extension of two charters in 1814, required each bank to lend up to one-tenth of the capital. In South Carolina, in 1822, for charter extension, a bonus of \$20,000 was demanded.

^a Lewis, *History of the Bank of North America*, p. 91.

^b Bryan, *History of State Banking in Maryland*, p. 28.

^c *Ibid.*, p. 49.

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The experience of Alabama illustrates the way in which some of the new States became dependent upon the banks for loans. This State was admitted into the Union in 1818, a time of financial stringency; settlers were purchasing public lands and a large number of citizens were indebted to the Federal Government for these lands, purchased on the installment plan. By the terms of agreement at the time of its admission to the Union, the State could not tax lands until five years after sale, and lands unsold were not taxable. Much of the land that could be taxed was being cleared for cultivation and had not reached its full value; receipts from taxation, therefore, were slight, and loans were necessary. At the very beginning of its organization, in December, 1819, the legislature authorized the government to borrow \$20,000 from the banks at Huntsville and St. Stephens for the use and benefit of the State.

The charter of the Bank of Missouri, 1817, gave the State the privilege of borrowing one-half of its stock holdings without giving receipts. The State Bank of Indiana, 1817, was required to loan up to \$50,000 for five years whenever authorized by law.^a

The Bank of Kentucky, though not required by law, readily responded to demands for loans in behalf of public improvements. In 1836 it loaned \$200,000 to the city of Louisville to pay its subscription to the stock of a railroad, and other similar loans were made.^b

^a Laws, Ind., 1817, ch. 41, sec. 11.

^b Duke, History of Bank of Ky., p. 49.

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XXV. LOANS TO SPECIAL INTERESTS.

In a few States, particularly in New England, the charters, during the earliest period, required banks to make loans to special classes in the community, as farmers or mechanics. The Plymouth Bank in Massachusetts, 1803, was required to appropriate one-eighth part of its capital "with exclusive regard to the agricultural interests and to loan this in sums not less than \$100 or greater than \$500 for not less than one year, to be secured by efficient mortgage." The same duty was imposed on the Worcester Bank, 1804. The State Bank in 1811 and the Suffolk Bank, 1818, both in Boston, were called upon to loan in small sums one-tenth of their capitals to the citizens outside of Boston who were engaged in agricultural or manufacturing pursuits. The same policy was followed in Maine. In 1802 one-eighth must be loaned to farmers, but in 1812 this was reduced to one-tenth.^a In Rhode Island, although bank charters did not set aside any specified portion of capital to be loaned to farmers, the need of the agricultural section for accommodation was given a prominent place in a few of the incorporations. In a preamble of the Rhode Island Union Bank, 1804, it is stated that the interests of the farmer had not been sufficiently consulted, "and the pledge of his real estate, which is the only security in his power to give, has not been accepted."^b

Though New York, as a rule, did not place specific obligations of loans to special classes upon her banks, there are

^a Stackpole, *Sound Currency*, 7:58-60.

^b Stokes, *Chartered Banking in Rhode Island*, p. 13.

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instances of responsibility which were recognized. The Bank of New York, for example, in 1792, at Hamilton's request, loaned \$45,000 to the Society for Establishing Useful Manufactures, organized in Philadelphia for the purpose of building factories in New Jersey, at a rate of interest at 5 per cent; Hamilton wrote, "In my opinion banks ought to afford accommodation in such cases upon easy payments of interest. I think 5 per cent ought to suffice where a direct public good is present."^a In October, 1793, the bank also made a loan of \$5,000 on the request of the mayor of New York City to "aid the poor and most distressed citizens of Philadelphia under a pressure of very great calamity."^b In their interest to serve mechanics, the legislature in at least three charters provided that a specified number of the directors should be mechanics. This was true of the Mechanics' Bank of New York, 1810, which was also required to devote \$600,000 of its \$1,600,000 of capital for the use of mechanics and tradesmen. The charter of the Mechanics' and Farmers' Bank of Albany, 1811, demanded that a majority of the thirteen directors should be practical mechanics; and that of the Tradesmen's Bank of New York, 1823, that thirteen of the twenty directors should be either mechanics, manufacturers, or selling goods of American manufacture.

By the charter of the New Jersey Manufacturing and Banking Company, 1823, manufacturers were entitled to preference to all others in respect to loans and discounts.^c

^a Domett, Bank of New York, p. 49.

^b Ibid., p. 50.

^c Private Acts, N. J., 48 Ass., 1 sess., p. 162.

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In 1809 Pennsylvania, in the charter of the Farmers' and Mechanics' Bank of Philadelphia, imitated Massachusetts, providing that one-tenth of the capital should be loaned to farmers if applied for, and in 1814 the legislature required that the new banks should loan not exceeding one-fifth of their capital, for one year, to farmers, mechanics, and manufacturers of their respective districts. This provision was repeated in the general banking law of March 25, 1824.^a

In addition to these examples of regard for particular classes in the community, the great state "property" banks in the South and Southwest should be referred to. These were designed primarily to make loans to farmers and planters, but were organized on principles entirely distinct from commercial banks.

XXVI. DEPOSITS.

During the earlier period of state banking individual deposits did not play an important part in banking business. Loans were taken out in bank notes rather than in the use of credit against which checks could be drawn. As Dunbar states, "Comparative sparseness of population and the imperfect development of the banking habit in a new and more slowly advancing country, and in a less advanced age than the present, created an early preference for currency which passes from hand to hand and discouraged the use of that which implies a resort to the bank."^b

^a Article xxiv, sec. 8.

^b Dunbar, *Economic Essays*, p. 174.

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After 1840 there began to be an increase in deposits and a relative decrease in the use of bank notes. In that year deposits, for example, in New York amounted to only \$16,100,000, but by 1860 they had increased over sevenfold, while capital and circulation increased only threefold. Specie holdings were about four times as much, but if the great increase in demand obligations of depositors is considered, this increase was entirely inadequate. In 1857, when the panic occurred, the specie reserve amounted to only about 13 per cent of the combined obligations of depositors and note holders. It was then realized as never before that deposits constituted a liability which it might be extremely difficult to meet in times of a crisis. Already the practice had grown up of the payment of interest by banks both on demand deposits to individuals and on country bank balances.

In 1859 the bank superintendent of New York reported that the business of the country had ceased in a very considerable degree to be transacted through the medium of bank notes; facilities were now so convenient for cash, checks, and drafts that bank accounts had come into general use. It was estimated that within ten years the number of depositors had increased twenty times.

In 1820 in a bank investigation in New York, an attempt was made to learn whether interest was allowed at that time by city banks to country banks on their balances. One of the witnesses stated that he thought the Bank of America paid interest to the Planters' Bank

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of Georgia; another stated that he knew of such accounts but was unable to give specifications; and a third said that he never knew of such a practice. Within a few years, however, the practice became general, although frequent efforts were made to do away with it. In 1852 the New York City banks generally agreed to abolish the practice of allowing interest on country bank deposits, but the agreement was not kept.^a The bank superintendent of New York, in 1857, condemned the practice; it attracted large amounts from outside banks which were practically demand loans; because of this the sudden suspension of specie payments in 1857 was largely due.

In Massachusetts frequent efforts were made to break up this practice. The subject was discussed by the bank commissioners in their report of 1839; in 1840 they stated that some of the individual deposits bore interest, but, in 1851 the commissioners reported that in that year they had not met with any instance of interest on individual deposits.

The commissioners of Rhode Island in 1836 reported, that interest was paid by some of the banks, but generally on small sums not exceeding 5 per cent. The commissioners of Maine in 1862 stated that a few of the banks allowed interest of from 3 to 5 per cent. The commissioners of Connecticut in 1854 complained that banks resorted to the practice of borrowing money in the form of deposits at rates from 4 to 6 per cent and then loaning it at advanced rates. This practice was questioned, since it

^a Merchants' Mag., 38: 328; Senate Report, No. 58, February 29, 1856.

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tended to concentrate the surplus capital at points where the banks were located. If the money thus deposited was loaned outside the State it was detrimental to business. It was a wide departure from the true principle of banking and invited and encouraged large deposits. A law was consequently passed limiting the rate of interest on deposits, but it was repealed in the next year. In 1862 the commissioners reported that the practice of paying interest was generally discontinued.

The charter of a bank organized in New Jersey in 1834 specially provided that 3 per cent interest should be allowed to special depositors. These funds, however, were not to be withdrawn for sixty days.^a

XXVII. SPECIE RESERVE.

After 1837 the question of having an adequate specie basis to support circulation became a matter of common discussion. Practically the only provisions relating to the holding of specie were those requiring original payments in gold and silver of a certain portion of the capital stock before the bank began business, but, as a rule, banks did not retain this coin after operations were once begun. Another indirect requirement was that which prescribed a penalty in case a bank refused or delayed redemption of bills. In these provisions it will be observed, however, that there was no specification of keeping on hand a fixed amount.

In Massachusetts the joint committee on banks and banking in 1840 reported that it would be unconstitutional to impose upon banks the requirement that they

^a Acts, 58th Assembly, p. 148, sec. 18.

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should keep on hand 10 per cent in specie, as this would be a new burden not contemplated in the original charters. In 1850^a the subject was again investigated by the legislature, but a committee again thought that application of a definite rule was too difficult to determine; there was a great variation in the amount of specie kept by individual banks; in Plymouth County banks varied in their circulation as compared with specie from 16 to 24; in Norfolk County, from 6 to 30; in Middlesex, 5 to 41; in Suffolk, in which Boston is located, from 1 to 42; in Bristol, 6 to 64.^b In 1855 the bank commissioners reported that the banks kept too little specie; country banks with a capital of more than \$26,000,000 had but about \$1,000,000 in specie, and the city banks with a capital of \$33,000,000 had an average of only about \$3,000,000.^c In the next year the commissioners again referred to the subject and noted that the banks had not improved their position: "We continue to feel surprised that judicious men connected with banks still continue to speak with indifference of the item of specie."^d

In 1858 an act was passed requiring the banks to keep on hand in specie 15 per cent of their aggregate liability for circulation and deposits. Banks outside of Boston, however, could count as specie their balances in other banks, not bearing interest, which could be applied to the redemption of bills. Under this proviso a country bank was not obliged to keep a dollar in its own vaults,

^a See Senate Document, Mass., No. 6, 1850.

^b Merchants' Mag., 37:183.

^c Fifth Report of the Bank Commissioners, Mass., 1855, p. 76.

^d Sixth Report of the Bank Commissioners, Mass., 1856, p. 78.

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and such exceptional favor met with the disapprobation of the bank commissioners, who thought that at least 5 or 10 per cent should be kept by the bank itself.^a The bank commissioners had originally proposed that 20 per cent should be kept. The bill was passed against great obstacles in the face of the hostility of the country banks, and in order to secure its passage it was obliged to make the above concessions. Balances in New York banks were also allowed to be counted on the same footing with those in Boston, a concession to meet the practice of some banks in the southern and western parts of the State whose balances were kept more largely with New York. The restriction that specie balances must not draw interest was removed by the legislature in 1859 on the ground that the payment of interest forced the city banks to extend their loans in order to meet the expense. Under these exceptions and modifications the specie reserve was practically no higher than it was in 1825, and consequently did not prove as beneficial as it was hoped.^b Another point to be taken into consideration in judging this legislation is that the specie which was held by Boston banks did duty not only for Massachusetts, but for the whole of New England, inasmuch as the banks of the other states had their currency daily redeemed in Boston. In 1860 the aggregate circulation of the five States in New England other than Massachusetts was \$22,500,000, while the specie was only \$2,500,000; if to this be added the deposits of \$14,500,000 and the liabilities of Massachusetts banks be taken into account, there

^a Eighth Report of the Bank Commissioners, Mass., 1858, p. 95.

^b Report of Bank Commissioners, Mass. 1860, p. 125.

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was a total of nearly \$90,000,000 of liabilities protected by only \$9,500,000 of specie.^a This law gave rise to a new abuse, the borrowing of specie by one bank from another in order to enable it to make up its legal average, and this practice was said to be much resorted to by banks in Boston.^b In 1861 the average specie holdings of the country banks was only 7½ per cent and of the Boston banks 21 per cent.^c It is also to be noted that many of the Boston banks did not in individual weeks show a legal reserve. One bank, for example, was below the legal average in thirty-four out of the fifty-two weeks in the year, while six others were below the line for twenty weeks or more.^d Massachusetts therefore did not have a preeminent record, as judged by specie holdings of her banks; for the five years ending with 1820 the average of specie was 23 per cent; for the period ending with 1825 the average was 20 per cent; 1830, 17 per cent; 1835, 8 per cent; 1840, 12 per cent; 1845, 21 per cent.

During the four years succeeding 1857 the proportion fell to less than 9 per cent, which was not much more than the low standard of 1837. The specie reserves of Massachusetts banks were lower than those of the whole country taken together; for all the United States, the reserve never fell below 13 per cent, while in Massachusetts in 1835 it fell to 7½ per cent.^e

In 1846 Maine passed a law which gave a specie basis to the circulation, and in 1857 every bank was required

^a Tenth Report of Bank Commissioners, Mass., 1860, p. 126.

^b *Ibid.*, p. 124.

^c Eleventh Report of the Bank Commissioners, Mass., 1861, p. 150.

^d *Ibid.*, p. 148.

^e *Ibid.*, p. 147.

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to keep at least 5 per cent in specie in its own vaults. In Connecticut, as early as 1838, the bank commissioners recommended that circulation be based upon specie, and in 1841 the proportion of one-third was suggested. In 1848, 10 per cent was recommended, for this would not be a hardship on many of the banks, as most of them had more than that amount of specie on hand. A law was subsequently passed requiring 10 per cent of the circulation to be kept in specie.

In Rhode Island a legislative committee in 1826 reported that it was a well-settled principle in banking "that every well-conducted bank, even though it confined its advances to the discount of commercial paper or to bills of exchange at short dates, must have always on hand one-third or as much as one-half of the total amount of its circulating paper." Although some believed that Rhode Island banks could do as well with a much smaller proportion, as one-fourth or one-fifth, such a policy was not approved, since banks must be provided against emergencies. Taking all banks together, the specie was more than a third of the notes, but there was a great difference in Rhode Island in the amount of circulation put forth by commercial banks and other banks. Eight commercial banks, for example, with a capital of \$2,931,000, had only \$218,000 in notes, with \$183,000 in specie; and twenty other banks, with a capital of \$795,000, had \$466,000 in notes and only \$156,000 in specie. Under the operations of the Suffolk system of redemption there was a constantly decreasing amount of specie, and it ceased to play an important part as a basis of circulation and was treated rather as a reserve.

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Country banks in New York kept but a small amount of specie; about 1820 amounts ranged from one-eighteenth to two-sevenths of the combined notes and deposits. Eleven city banks in 1829 had one-seventh of their demand obligations in specie, while the same number of country banks had only about one-twentieth. This, however, did not include the sums which country banks kept with the city banks to meet obligations for note redemptions. The bank commissioners in 1833 called attention to the small specie reserve, less than \$2,000,000 for a circulation of \$12,000,000, and warned the legislature of the danger. Under the bank act of 1838 each banking association was required to keep 12½ per cent of its circulation in specie. This provision, however, was repealed in 1840, but the comptroller of the State in the following year reported upon the necessity of increasing the specie basis. This could be done in one of two ways—by suppression of small bills or by increasing the specie. A reserve of 20 per cent of the circulation in specie was favored. Nothing was done, and for years, with the growing importance of New York City as a commercial center, the weak state of the specie reserve excited comment.^a For two years, 1853–1855, banks made voluntary agreements to keep an average of 20 per cent of specie on their weekly balances, but this was abandoned.

The panic of 1857, however, brought into new prominence the need of conservative practice, and in March, 1858, the city banks made an agreement “to keep on hand at all times an amount of coin equivalent to not less

^a See Merchants' Mag., 25:152.

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than 20 per cent of our net deposits of every kind, which shall be made to include certified checks and other liabilities except circulating notes, deducting the daily exchanges received from the clearing house." (Report of Comptroller of the Currency, 1873, p. xxiv.)

Although there was little legislation in States south of New York on this subject, the need of a better protection to the circulation through the holding of coin was frequently referred to by the bank commissioners and legislative committees. Not, however, until 1860 was there any specific requirement as to specie holdings by banks in Pennsylvania, and in the law then passed only 8 per cent in specie or its equivalent was demanded.^a In Maryland, a legislative committee in 1837 reported that the ratio of circulation to specie was less than the healthy and authorized proportion of 3 to 1. A committee of Virginia, about 1835, stated that it was difficult to determine how much specie a bank should have in order to redeem its notes—the estimate was usually of 3 to 1, but in Virginia the actual ratio was \$5.22 to \$1. An act in 1837 provided that banks should have one-fifth of their notes in specie and forbade a bank to make any loan when the reserve fell below this limit.^b This ratio was observed in subsequent legislation.^c Alabama, in 1837, enacted that the Bank of the State of Alabama should have one-fourth of its capital in specie by July 1, 1841.

^a Pub. Laws, Penn., 1860, p. 459.

^b Laws, Va., 1836-37, ch. 82, sec. 3.

^c Laws, Va., 1850-51, ch. 58, sec. 10; Laws, 1855-56, ch. 60, sec. 4; ch. 61, sec. 4; ch. 63, sec. 4.

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In 1838 the bank commissioners of Mississippi advised that the banks should have \$1 in specie to every \$3 in circulation and deposits. Louisiana had the credit of taking the most advanced position of all the States in her reserve requirements for banks; for many years the Louisiana State Bank maintained a specie holding of one-third of its total responsibilities. In 1838 the associated banks of New Orleans agreed to carry, in 1839, specie holdings of one-third of their cash responsibilities. In 1846 the banking law of Louisiana required the banks to hold one-third of their aggregate circulation and deposits in specie, while a sum equal to the remaining two-thirds must be invested in short paper payable absolutely at maturity. Discounting by a bank which had been ten days below the specie line was made an act of insolvency, requiring liquidation, and directors or managers who assented to the violation of the law on this point were made individually liable for all debts. This legislation was approved by its results; banks of New Orleans passed successfully through the crisis of 1857, and in March, 1861, at the beginning of the civil war, they held sixteen millions of specie to a capital of twenty millions.

Ohio, in 1839, enacted that the volume of bills issued should not exceed three times the amount of specie on hand, exclusive of deposits.^a By the free-banking act of 1851 banks were required to have on hand in gold or silver, or their equivalent, 30 per cent of their outstanding notes. The State Bank of Iowa, 1858, required a reserve of coin of one-fourth of the circulation and a similar reserve in current notes for the deposits.

^a Rev. Stat., Ohio, 1841, p. 126.

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XXVIII. SURPLUS.

Only in a few instances did banking laws during the early period provide for a surplus. If there was any decided opinion, it was apparently adverse to a bank's accumulating large funds in excess of capital, due to the fear of large moneyed corporations.

Connecticut, in 1835, passed a general law forbidding any bank to retain as surplus more than 5 per cent of its paid-in capital. Three years later, however, this act was repealed.^a In 1846 the bank commissioners stated that banks should not be allowed to accumulate a large surplus, as it would tempt those who knew the true condition of the bank to take advantage in the purchase of stocks of those who were less well informed; but in 1849 they reported that banks should be encouraged to create a surplus, so as to make dividends uniform.

Maryland, in the charter of the Mechanics' Bank, 1806, permitted the management, if it desired, to retain at least 1 per cent of the capital from surplus profits as a contingency fund. This was common in other charters, but not in all.^b Virginia, in the charter of the Merchants' and Mechanics' Bank, 1834, required the laying aside of \$10,000 surplus before the payment of more than 6 per cent dividends.^c In 1837 all banks in that State were required to maintain a surplus of at least 5 per cent, not exceeding, however, 10 per cent of the capital, before paying dividends. This was known as a "contingency

^a Woodward, *The Hartford Bank*, 137.

^b Bryan, *State Banking in Maryland*, 33.

^c *Laws, Virginia*, 1833-34, ch. 72, sec. 10.

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fund."^a In 1852 it was enacted that banks should not pay over 6 per cent dividends until 1 per cent of the capital had been carried to surplus, to be continued until the total surplus equalled 5 per cent.^b

Florida, in a charter of 1845, limited dividends to 10 per cent, and required the excess profit to be set aside as a safety fund. The Franklin Bank of Cincinnati, 1833, permitted no dividend of more than 3 per cent to be paid until the bank had a surplus of \$30,000. The charter of the Bank of Kentucky, 1834, provided that no dividend should be declared until there was a surplus of \$20,000 for every million dollars of stock.^c By the charter of the State Bank of Indiana, 1834, each branch was required to set aside one-sixth of its capital before dividends were paid.^d

^a Laws, Virginia, 1836-37, ch. 82, sec. 6.

^b Laws, Virginia, 1851-52, ch. 120, sec. 4.

^c Duke, History of the Bank of Kentucky, 38.

^d Laws, Indiana, 1834, ch. 7, sec. 54.

The Safety-Fund Banking System in New York State, 1829-1866

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THE SAFETY-FUND BANKING SYSTEM IN NEW YORK

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THE SAFETY-FUND BANKING SYSTEM IN NEW YORK STATE: 1829-1866.



CHAPTER I.

BANKING EXPERIENCE BEFORE 1829 IN NEW YORK.

At an early date in New York State banking was restricted and the privilege made an exclusive grant by special legislative charter. A combination of circumstances brought this about. The community had vivid recollections of losses sustained under the colonial banking systems with their excessive and inconvertible issues of paper currency. The impression was common that banks were combinations of the rich against the poor, and should be strictly regulated by the people's representatives. But before many years had passed the granting of special bank charters had been carried into politics and it became the interest of the party in power to compel all banking to be done through these chartered corporations.

The Bank of New York had been formed by Hamilton in 1784, but was not able to secure a charter until 1791. This first bank in the State was thus compelled to carry on its business for seven years before the legislature would grant it a special charter. In the following year the Bank of Albany was chartered, and in 1793 the Bank of Columbia at Hudson. So far the needs of the com-

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munity, and not politics, seem to have guided the legislators. Until 1799 only \$1,600,000 was employed in banking.

Now politics in New York State grew more intense. It so happened that the stock and management of the Bank of New York were in the hands of the Federalists. The Republicans, led by Burr, claimed that the bank discriminated in favor of Federalists, and he devised a scheme for incorporating another bank in New York City. The legislature was Federalist and, therefore, the only hope for another charter was to deceive the members as to the real purpose of the new corporation. This Burr proceeded to do at the session of 1799. The city was in need of a supply of pure water and the public realized this fact. The legislature was, accordingly, asked to charter, on the most liberal terms, a company which would undertake this great public work. But it was not certain how much capital would be required, so in the charter the authorization was asked for and granted that the company be permitted to procure \$2,000,000 capital and then use any surplus not needed for the water-supply business "in any way not inconsistent with the law and Constitution of the United States, or of the State of New York."^a The majority of the legislature did not know that they were granting perpetual banking powers, but such was the purpose to which the new company devoted its surplus.

At the session of 1803 the application for a charter for the New York State Bank at Albany assumed a politi-

^a Hammond, J. D.: *The Hist. of Polit. Parties in the State of New York*, 3d ed, 1845, Vol. I, p. 326.

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cal character. The applicants claimed that the Bank of Albany belonged to Federalists and that it discriminated against Republicans. They advocated the bank in the interests of the public while they attached to their application a scheme of speculation and private gain. This charter passed the legislature, but two other companies, the Merchants' Bank of New York and the Mercantile Company of Albany, failed to secure charters. The charge was at once made that influential men connected with existing banks, and interested in the monopoly thus formed, prevented the further creation of banking corporations. At any rate, the next legislature, instead of incorporating new banks, passed the restraining law of 1804, which had been recommended by a committee of the assembly, consisting of one member from each county. This law prohibited associations of persons from banking and placed a fine of \$1,000 on any individual becoming a member of such an association, but did not prevent individuals or incorporated institutions from engaging in banking and issuing notes.^a Notes were issued of various denominations, as low as 6 cents in value, by the Bankers' Exchange Bank, the Utica Insurance Company, the Little Falls Aqueduct Association, and such individuals as Calvin Cheeseman, besides many tavern keepers, merchants, and turnpike companies. A further restraining law was passed in 1818 effectively preventing private banking or note issue until 1837, when it was repealed, except that private bankers were not permitted to issue notes for circulation as money.

^a See semiweekly Albany Argus, Dec 20, 1836: Article on the "Restraining Law," over name "Franklin."

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In a debate on the renewal of bank charters in the session of 1827, the speaker of the house asserted that the profits of city banks "do not depend upon the circulation of their bills, but arise from the discount of notes." This emphasizes a difference between the city and country banks which has been marked at all periods of our history, but especially during the early years when the deposit and check system of banking had nowhere developed to such a great extent as at present, and when deposits were an insignificant item in the statements of the country banks. Therefore the speaker goes on to point out in the same speech that the profits of country banks in 1827 depended on the quantity of bills kept in circulation.^a The city banks had larger deposits and capitals on which to extend discounts and consequently made less use of note issue. Since note issue was the chief function of most country banks, the chief concern of legislation was to protect the note holders from losses through bank failures, or from depreciation of bank paper by overissues. We must keep this fact in mind all through this discussion in order to understand the course of legislation.

Not many of the banks were required by their charters to report to the legislature regularly, but from those that did so report the following items show the kind of banking business done by country banks.

^a Argus Supplement, Mar. 9, 1827.

Reports of banks to the New York assembly.

1820. ^a

	Debts due bank for discount, loans, etc.	Capital subscribed.	Capital paid in.	Notes.	Deposits.	Specie.
(1) Greene County Bank	\$79,651.60	\$90,000.00	\$43,669.30	\$20,334.00	\$14,440.35	-----
(2) Washington and Warren Bank	305,977.35	400,000.00	176,218.75	186,059.00	201.30	\$10,000.00
(3) Bank of Geneva	235,201.52	400,000.00	100,000.00	187,625.00	21,536.46	27,257.75

^a Assem. jol., 1820, pp. 468-469.

1824.

(1) Central Bank	\$113,221.18	\$200,000.00	\$45,000.00	\$128,717.00	\$9,887.36	\$22,136.76
(2) Bank of Plattsburg	188,379.94	300,000.00	60,000.00	188,643.57	21,467.08	18,076.74
(3) Bank of Geneva	425,482.79	400,000.00	175,000.00	418,155.00	49,025.21	50,399.37
(4) Greene County Bank	126,167.15	90,000.00	42,669.30	116,367.50	25,155.39	7,773.04
(5) Bank of Auburn	207,447.59	-----	143,928.00	155,341.00	27,603.39	51,841.17
(6) Washington and Warren Bank	291,966.12	-----	176,218.75	89,750.00	-----	-----

^b Assem. jol., 1824, pp. 273-276.

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These reports, as above stated, do not show the full resources of the banks, for the cash items, consisting of deposits with banks in Albany and New York to meet the redemption of notes and payment of drafts, etc., as well as the notes of specie paying banks, are not recorded, nor is the value of real estate belonging to the bank estimated. But the reports do show, first, that only one-fifth to nearly one-half of the subscribed capital had virtually been paid in, and also that the profits of these country banks depended very largely on their notes in circulation, the notes in almost every case largely exceeding the amount of capital paid in, and about equaling the debts due to banks for discounts, loans, etc. The reports also show that very little specie was actually kept in the vaults with which to redeem notes and pay deposits, the amount ranging from one-eighteenth to two-sevenths of the combined notes and deposits. It may be said, however, that the cash items kept on deposit at New York and Albany for note redemption should be counted in the reserve for notes, which would raise the percentage considerably. It is also clear from the reports how small a part of the total business of these country banks consisted of deposits.

A more elaborate report of 22 banks was gathered and presented to the state senate by the committee of which Senator Allen was chairman, January, 1829.^a This report includes eleven banks in New York City and Albany as well as the same number of country banks and will throw additional light on banking conditions, especially the contrast between city and country.

^aSen. jol., 1829, pp. 81-84.

CITY BANKS.

Bank	Notes dis- counted and loans.	Capital paid in.	Notes.	Deposits.	Specie.	Balance due from banks.
(1) Mechanics and Farmers' Bank, Albany.	\$1,017,962	\$312,000	\$325,000	\$396,774	\$26,000	\$170,053
(2) Bank of Albany	484,077	240,000	100,700	151,018	30,261	
(3) New York State Bank, Albany	791,814	369,600	178,002	359,707	30,976	94,202
(4) City Bank, New York City	1,267,033	1,000,000	244,904	219,215	66,806	47,711
(5) Union Bank, New York City	1,252,840	1,000,000	200,320	222,068	45,754	113,890
(6) Bank of America, New York City	2,328,074	2,031,200	221,884	332,238	184,610	206,480
(7) Mechanics' Bank, New York City	2,848,898	2,000,000	607,105	755,794	199,114	432,356
(8) Merchants' Bank, New York City	2,083,298	1,463,000	574,325	625,992	222,396	308,779
(9) Tradesmen's Bank, New York City	743,454	363,160	198,140	248,046	33,357	54,428
(10) New York Bank, New York City	2,904,991	1,973,200	540,955	796,912	99,978	349,641
(11) Phoenix Bank, New York City	980,026	500,000	337,288	340,324	79,078	175,108
Total	16,702,467	11,252,160	3,528,623	4,448,088	1,018,330	1,952,648

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COUNTRY BANKS.

Bank.	Notes discounted and loans.	Capital paid in.	Notes.	Deposits.	Specie.	Balance due from banks.
(1) Jefferson County Bank.....	\$109,343	\$74,000	\$94,545	\$18,921	\$14,113	\$66,012
(2) Bank of Utica.....	1,198,799	500,000	607,046	176,041	25,500	83,541
(3) Bank of Geneva.....	489,522	300,000	372,654	128,248	30,745	319,602
(4) Ontario Bank.....	1,118,987	500,000	500,944	267,776	28,937	186,064
(5) Farmers' Bank.....	618,433	278,000	153,397	79,686	11,660	-----
(6) Bank of Troy.....	948,660	352,000	326,379	96,394	10,533	-----
(7) Mohawk Bank.....	273,080	165,000	78,128	83,893	12,941	16,947
(8) Bank of Auburn.....	228,393	143,928	264,630	49,470	30,455	200,909
(9) Middle District Bank.....	567,807	397,485	293,750	45,288	15,684	155,656
(10) Catskill Bank.....	414,747	110,000	274,510	80,940	7,965	39,900
(11) Central Bank.....	217,749	86,000	171,527	16,208	18,096	58,493
Total.....	6,185,520	2,906,413	3,137,510	1,042,865	206,629	1,127,124

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The committee regarded all the above reports as satisfactory and as proof of the "sound state of our circulating medium." They regarded it as a cause of congratulation that in forty years since state banks began to be chartered only five had suspended payment of their notes. There were no data of losses to the public from these failed banks, but the capital was small.^a

The above reports, with their summaries, show the essential differences in the banking business as carried on in the country and city. It will be noticed, of course, that the capital employed in the city banks is almost four times as great as in the same number of country banks, while the notes issued are about the same in amount. The deposits of the city banks are about four times those of the country banks and the specie on hand about five times. A larger relative amount of specie was necessary in the city banks to meet the greater demands there. The table shows that the city banks depended upon their paid-up capital and their deposits for their ability to discount and loan rather than upon their credit in the form of bank notes. The amount of notes in circulation is less than a third of the capital and only about three-fourths of the deposits. In the country banks, on the other hand, the paid-up capital, instead of being two-thirds of the loans and discounts, as in the case of the city banks, is less than one-half of the loans and discounts. The notes in circulation exceed the capital and are three times the amount of deposits, which again is in marked contrast to the city banks. The notes, in-

^aSen. jol., 1829, p. 79.

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stead of being about one-fifth of the loans and discounts, as in the case of the city banks, amount to more than one-half. The city banks held on hand about one-seventh of the demand obligations of notes and deposits in specie, while the country banks held only about one-twentieth. The large balance due from banks shows that the country banks kept large sums with the city banks to meet obligations for note redemption, drafts, etc. The table as a whole shows too small proportion of specie as a basis for a sound banking system, and in the case of the country banks too much dependence upon note issue as a source of profit. All these facts must be kept in mind when we discuss the safety-fund law of 1829. Thus will the opposition of the city banks be explained.

Since the granting of a bank charter by the legislature had become a matter of party politics, charges of corruption were frequently made and in some cases proven. It was to the interest of existing banks to keep rivals out of the field, and those who sought charters used various means to win over legislators. Stock was distributed to members with the promise of an immediate market at a premium.^a Granting of a bank charter was linked with various forms of special legislation, and log-rolling was encouraged. The party in power could make the distribution of bank stock a part of the spoils of political victory. These evils were all inherent in the system of granting bank charters by special legislative act, which did not always result in placing a bank where the needs of the business community demanded or in securing the investment of *bona-fide*

^a Hammond, Vol. I, pp. 332-337.

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capital in the institution when chartered. Previous political corruption and scandal influenced the convention of 1821 to place a clause in the constitution requiring a two-thirds vote of the legislature to pass a bank charter. They hoped thus to avoid the log-rolling and bargaining, but as a matter of fact the effect was "to increase the evil by rendering necessary a more extended system of corruption."^a A bonus was sometimes demanded by the legislature in return for the grant of a charter. The result of this policy is shown by a memorial of the Fulton Bank of New York City protesting, in 1833, against being subjected to the safety-fund law, on the ground that it had already paid a bonus of \$133,000 when its charter was granted in 1824, and therefore should be exempt from the tax of one-half per cent imposed by the law of 1829. This alleged bonus was paid by allowing the trustees of Daniel D. Tompkins, who had a claim upon the legislature for patriotic services, to subscribe for \$150,000 in stock and pay for the bank stock with the stock of the Richmond Turnpike Company at par. The stock of this turnpike company netted the bank only \$17,000.^b

An examination of these early charter provisions will show how sound banking develops slowly out of experience. The charters from 1800 to 1825 show certain common provisions to which others were added as experience dictated. Among these we find the limitation of the bank in ownership of real estate and trading in goods or stock, certain specifications as to qualifications and election of directors, the requirement of registration for a valid trans-

^a Hammond, p. 337.

^b S. Doc. 104, 1833, Vol. II

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fer of stock, the regulation of the total debts, exclusive of the specie actually on hand, to three times the paid-up capital, and the personal liability of the directors, who were responsible for the excess unless absent or dissenting. The maximum interest rate for short loans was fixed at 6 per cent.^a It will be observed that there is as yet no enumeration of banking powers specifically granted, no uniform requirement for reports or provision for inspection, no provision for paid-up capital before opening for business, no reservation of the right of the legislature to modify or repeal the charters granted, and no satisfactory method of distributing the bank stock.

In chartering the Union Bank, as well as two other banks, in 1811, the legislature appointed the first directors,^b but the charter of the Middle District Bank, granted in the same year, provided for commissioners named by the legislature to distribute the stock and arrange the first election of directors.^c This latter method, by commissioners, continued^d to be followed under the safety-fund system for several years and was the source of much complaint and abuse.

In 1811 the requirement was made that the business of the bank should be carried on at the place specified in the charter and not elsewhere, and that stock must be held a certain time before election of directors in order to entitle the owner to a vote. A limitation was placed in the charter regulating the amount which the president or any di-

^a Session Laws, 1805, chap. 43.

^b Session Laws, 1811, chap. 34.

^c *Ibid.*, chap. 68.

^d *Ibid.*, chap. 46.

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rector might owe the bank at any one time for loans and discounts, and preventing any person from being officer or director in more than one bank. Directors or officers must not purchase notes or bills at usurious rates, and the cashier and clerks must give bonds.^a

In 1824, in chartering the Bank of Rochester, the legislature required an oath, by the president and cashier, that 25 per cent of the capital had been actually paid in, half in specie and half in current notes, before the bank could legally issue its own notes.^b This amount was increased to 50 per cent in 1825 in chartering the Commercial Bank of Albany.^c Therefore, before the safety-fund law of 1829 it was not necessary to pay in more than 50 per cent of capital subscribed before beginning business, and in some banks only 12½ per cent was required in specie.

During 1824, in a bank charter, a penalty was placed upon failure to redeem notes on demand, and it was made the duty of the president and cashier to report to the Comptroller under oath annually the condition of the bank, specifying the items required, and the right "to alter, modify or repeal" the charter was reserved.^b

In granting a charter to the Commercial Bank of Albany in 1825 the act enumerates expressly the banking powers, and continues, "but the said company shall have and possess no other powers whatever, except such as are expressly granted by this act." This is the first charter found where such powers were enumerated. The bank was also prohibited from receiving the transfer, pledge or

^a Session Laws, 1811, chap. 64.

^b Session Laws, 1824, chap. 46.

^c Session Laws, 1825, chap. 117.

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hypothecation of any stock of the bank itself or of any other incorporated company. At the opening of the bank the affidavit of the president and cashier must state that no loans had been made, as far as the officers knew, to enable any stockholder to pay the amount of his shares under any implied or express agreement that such loans were to be repaid by a discount of any note or other security by the bank. The charter prohibited the directors from dividing as dividends or paying to the stockholders any part of the capital stock or reducing the capital without the consent of the legislature. It was made illegal to discount or receive any note in payment of any part due upon stock of the bank, or to enable stockholders to withdraw money paid on stock. Directors were made personally liable for amounts thus withdrawn or discounted. The president or directors who violated these provisions, as well as those with reference to the total legal debt allowed, were guilty of a misdemeanor and liable to fine of \$1,000 and three years' imprisonment, or either. In the annual report the president and cashier must take oath that the specie on hand is *bona fide* the property of the bank "and has not been borrowed or in any wise obtained with a view to make the return."^a These charter provisions have been stated in some detail to show the necessary growth of restrictions in the charters to remedy certain evils that developed. The provisions above stated indicate clearly what those evils were and need no comment. But the fact to be emphasized is that all these

^a Session Laws, 1825, chap. 117.

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provisions must be inserted in every bank charter if they were to be effective for the particular bank.

Bank charters granted and capital authorized, 1791-1825.^a

Period.	Additions to bank capital by charters.	Aggregate capital authorized.
1791-1810 (inclusive).....	10	\$7,430,000
1811-1818 (inclusive).....	23	17,290,000
1821-1825 (inclusive).....	10	4,300,000

^a Assem. Doc. 102, 1836, Vol. II.

During the first period not more than one bank charter was granted in any single year. It was a time of conservative banking, with no failures. With the expiration of the charter of the first United States Bank there was a rapid increase of state banks, as shown for New York State in the above table. These figures do not include reductions made in bank capital by failures or voluntary reductions during the period, nor do they indicate the amount actually paid in and employed, but only the amounts authorized by charter. It will be observed that the period of greatest activity was during and after the war of 1812. The period following this war was characterized by more reckless banking and by speculation. During the two years, 1824 and 1825, eight of the ten additions were authorized, but no more charters were granted until after the safety-fund law was passed in 1829. Of the ten incorporations during the first period in the above table, there were only two failures and those were during the period following, but of those organized in the second and third periods there were six failures. The information as to causes of failure

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and the affairs of the failed banks, before the safety-fund system was inaugurated, is too inadequate to allow conclusions, but the failures were probably due to the evils indicated in the provisions of the later charters, just stated above.^a

The governor, in his message in 1818, describes the evils of a disordered currency which are "aggravated by the banking operations of individuals and the unauthorized emissions of small notes by corporations." He cautions the legislature against allowing the incorporation of banks in places where they are not required by trade, because such banks have few deposits and must rely upon note issue for profit. These notes are diffused by loans or by appointing agents to exchange them for the notes of other banks. They grant discounts liberally, but the apparent business activity is deceptive; there is a struggle of rival banks to redeem their notes, and to do this they must call in loans and embarrass borrowers. "The banishment of metallic money, the loss of commercial confidence, the exhibition of fictitious capital, the increase of civil prosecutions, the multiplication of crimes, the injurious enhancement of prices, and the dangerous extension of credit are among the mischiefs which flow from this state of things."^b

The report of the committee on banks of the assembly, during the same year, gives us more concrete examples of the abuses to which the governor referred. They refer to speculation in banking and declare that banks "enable the

^aCf. L. Carroll Root: "New York Bank Currency," *Sound Currency*, Vol. II, No. 5, p. 3.

^b *Assem. Jol.*, 1818, p. 15.

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designing, unprincipled speculator to impose on the credulity of the honest, industrious, unsuspecting part of the community—examples of this sort are too common and notorious to need any illustration.”^a The committee cites various schemes of banks to force their notes into circulation. Banks sometimes give accommodations to an individual on condition that he will pay the note when due in current money, meaning the current notes of other banks. This compels the borrower to lay aside current money during the time his note is running in order to be able to pay at the end of the time and often makes it necessary to borrow, at a high rate of interest, any balance that he does not possess when his note becomes due. Some banks lend on condition that the borrower leaves one-half the sum in the bank until the note is due, thereby receiving usurious interest. Merchants, who have payments to make abroad, stand the loss caused by depreciation of the bank’s paper rather than incur the bank’s resentment by asking for specie or current notes and thus losing the chance to secure accommodations at the institution. The committee reports a case of boycott where the board of directors of a bank passed a resolution declaring that “no man should hold a seat at that board, or receive any discounts at the bank, who should trade at a certain store in the same village, in consequence of the owner having asked for a sum less than \$4,000 in current money to remit to New York, while at the same time he kept his account in said bank.”^b The case is cited of a farmer who came to a bank for a

^a Assem. jol., 1818, pp. 307 et seq.

^b Ibid., p. 309.

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renewal of his note, indorsed by one of the directors, and this director charged him \$100 to aid him in securing the renewal.

The committee further gave its opinion that the circulating notes in the State were chiefly of the banks whose capitals were small and composed principally of the notes of individual stockholders called "stock notes." Therefore, the security of the note holders consists of the private fortunes of individual stockholders and those fortunes consist, in great measure, of the stock of the bank for which they have given their notes. This period of stock-note banking continued from the war of 1812 until the safety-fund law was adopted.^a

An assembly committee reported on the part of the governor's message which referred to banking and currency in 1819. They pointed out that so long as banks were established with reference to commercial and industrial needs they had been a blessing. But the success of banks and large dividends led to a clamor for bank charters. Banks were located where business did not demand and their multiplication was followed by excessive issues of bank notes without adequate means to redeem them.^b To keep these notes in circulation banks often placed obstacles in the way of prompt redemption.^c Distrust was thus created in the minds of the public. To get a renewal of a note at a country bank the borrower frequently was required to present the value of the note in

^a Cf. A. C. Flagg: *Banks and Banking in the State of New York, 1777-1864*, Brooklyn, 1868, p. 3.

^b Cf. Sen. jol., 1819, p. 68.

^c Cf. Assem. jol., 1820, p. 467.

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the notes of other banks for which the bank issued an equal amount of its own notes. This operation suppressed the circulation of other banks and extended the bank's own circulation.^a During the session of 1825 the legislature chartered several loan companies who proceeded to issue their bonds and pass them as money. This addition to the circulating medium contributed to the cotton speculation of 1826. About this same time corporate abuses were revealed in insurance and other corporations, which involved prominent New York business men.^b This increased the public alarm. The house in 1825 passed 18 bank bills with a capital of over \$7,000,000, but only 3 were finally chartered with a combined capital of \$1,150,000, because the house was checked by the senate.^c The house was called the "lobby assembly" during and after this session. The *Argus* describes this assembly as "alone in all the records of our country as the most subservient to the lobby and the most regardless of the public funds, the public interests, and the public will."^d

This legislature granted a charter to the Commercial Bank of Albany and appointed a commission to apportion the stock. The commission, it was alleged, appropriated to themselves and a few favorites a majority of shares of the stock. The merchants had been urged to subscribe, and then the stock was distributed largely to

^a Cf. *Daily Argus*, Mar. 29, 1825. Speech of C. D. Colden in the senate on a bill to allow private banking.

^b Willis S. Paine: *The Laws of the State of New York, Relating to Banks, Banking, etc.*, 5th ed., 1903, pp. 23-24, gives further details. Alarm in minds of public led to demand for the Revised Statutes of 1827.

^c *Daily Argus*, Apr. 29, 1825.

^d *Argus*, Oct. 23, 1826.

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others. They held a popular meeting to disapprove and passed resolutions declaring that the commissioners "had converted a matter of general interest and concern into an affair of individual profit and speculation."^a Such complaints were common, and this method of distribution of stock gave rise to serious evils. Sometimes it enabled a few men to control a bank for speculative or political purposes. They might borrow the specie needed to start business, pay dividends out of capital or redistribute the paid-up capital to the stockholders in discounts, and, under the appearance of prosperity, sell the stock at a premium. A number of bank failures before 1829 revealed the bad conditions of banking practice and destroyed the confidence of the public.^b This state of affairs went far to justify Senator Colden's criticism in the senate, in a speech on private banking, that most of the recent bank charters were granted not to those who wanted banks that they might lend money, but to those who wished to sell the stock at a profit.^c

At the opening of the session of 1827 notices were given of applications for 19 new bank charters and 23 renewals.^d The governor in his message cautioned the legislature against the evils of excessive issues of paper money and referred again to the forced and artificial circulation, with its train of evils. He recommended general regulations to restrict notes and to provide for

^a Albany Argus, June 14, 1825.

^b Pamphlet: *Origin, Provisions, and Effect of the Safety-Fund Law of New York State*. Albany, 1834, pp. 3 and 4.

^c Albany Argus, Mar. 29, 1825.

^d Albany Argus, Jan. 11, 1827.

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redemption and payment of debts, as well as to increase the responsibility of directors.

The Revised Statutes, adopted in 1827, on banking summarize the chief existing evils which the legislators sought to cure by general laws, rather than leaving the matters to specific provisions in each charter, as before. Most of the provisions are to be found in the most carefully restricted charters previously passed by the legislature and have already been noted. Article I is entitled, "Regulations to prevent the insolvency of moneyed corporations and to secure the rights of their creditors and stockholders."

It was made illegal for directors to pay dividends except from profits; to in any manner pay to stockholders any part of the capital stock or reduce it without the consent of the legislature; to receive notes of stockholders or make discounts in payment of capital stock; to receive from another corporation, in exchange for the shares, notes, or bonds of their own company, shares, notes, or bonds of the other corporation; to extend loans and discounts beyond three times the paid-up capital; and to loan or discount to the directors, or upon paper for which they stand responsible, to an amount more than one-third of the paid-up capital. A method of computing profits, from which alone dividends could be paid, was outlined, and, when losses exceeded these undivided profits, it must be considered an impairment of the capital and must be made good before further dividends could be paid. The law sought to prevent fraudulent transfer of the property of the corporation or a transfer to benefit

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particular creditors in case of contemplated or actual bankruptcy. If any director violates or is concerned in violating any of the above provisions he becomes liable personally to the creditors and stockholders to the full extent of the loss so sustained. Such director, whether loss results or not, becomes guilty of a misdemeanor and subject to a fine and imprisonment, or either. Every director is presumed to know about the affairs of his corporation, so as to determine whether any act or omission of his violates the provisions. If he dissents or is absent from the meeting where such violation occurs he must record his dissent, or he becomes liable with the others. Every insolvency is deemed fraudulent unless the affairs of the company appear on examination to have been fairly and legally administered. It is incumbent on directors and stockholders to repel by proof the presumption of fraud. In case of a fraudulent insolvency the directors by whose acts or omissions the failure was caused, wholly or in part, and whether then in office or not, shall be liable to the stockholders and creditors for their proportionate share of all losses. After the liability of the directors is exhausted in such a case, the rest shall be made good by the stockholders, to amount not exceeding the nominal amount of the shares held. Annual reports to the comptroller are required under oath of the president and cashier. No corporation may issue any bill or notes for less than \$1, to circulate as money. The directors and officers are prohibited from purchasing, directly or indirectly, any evidences of debt of the corporation for less than their

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nominal value. This prevented the purchase of their own bank notes at a discount. The directors and officers were also prohibited from discounting or loaning, directly or indirectly, upon paper which they knew to have been offered for discount to the directors or any officer and refused. This practice continued under the safety-fund system. Finally an affidavit was required by the two chief officers of the bank stating that the capital required by charter to be paid had been actually paid.

These provisions were stringent and meant to regulate improper practices, such as impairment of capital or stock-note capital, misuse of funds by officers or directors, and speculation. Personal liability was a recognized principle of the Revised Statutes.^a The provisions were not to be applied to corporations in existence January 1, 1828, but only to those charters granted or renewed after that date. But no more bank charters were granted until the safety-fund law of 1829 had been passed, which exempted corporations under it from the operation of sections 14, 15, 16, 17, and 18 so far as those sections provided for the personal liability of the stockholders of failed banks. The liability of directors to the stockholders was still retained as provided in these sections, but March 30, 1830, the legislature definitely repealed sections 11 to 18, inclusive. This repeal did not affect any existing bank or officer. Therefore, the banks chartered under the safety-fund law during 1829, about 27 in number, still retained the liability of directors, while the stockholders of these banks were free from personal

^a For text complete, cf. Revised Statutes of 1827, chap. 18, Pt. I, Title II.

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liability. Of course the directors of banks continued to be responsible for violations of the first nine sections of the statutes, but the requirement that they repel by proof the presumption of fraud was no longer operative and it was easy to evade the law, especially so long as there was no careful inspection by a regular official of the State.

In the debate on these Revised Statutes on banking the argument was advanced that such strict requirements and personal liability would drive men of capital and integrity from the banking business and leave it in the hands of irresponsible men and speculators. Parties for and against restriction were formed and the debate became warm between the opposing forces. When the safety-fund law came up for adoption a compromise was sought between the severe restrictionists and those who advocated perfect freedom in banking. It was supposed that the safety fund rendered unnecessary longer the severe provisions and yet afforded security to the public.

The evils we have observed so far in banking have been due either to a bad system, imperfectly guarded by needed restrictions; to official misconduct and lack of responsibility in management by officers and directors, or to the stage of business development at which banking had arrived in the process of working out a sound policy that would meet the test of prosperity, as well as of business adversity. Legislation had gone far to remove the evils of a bad system by requiring certain standards in banking and by the enforcement of greater responsibility upon directors, but to remedy the other evils was

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not always possible by legislation. Stockholders must learn by experience to hold directors to a more rigid accounting, and directors in turn must not allow themselves to become men of straw in the hands of designing bank officers of their own choosing. Safe methods of banking were only learned by long experience. The proper relation of a specie reserve to the demands and obligations of a bank was only gradually appreciated. Too much loaning was done on accommodation paper instead of on the evidences of past business transactions.^a The fact that note issue formed the chief source of profit to the country banks led to forcing notes into circulation, not necessarily in response to the demands of trade, but issued upon the notes of borrowers who came repeatedly to have their notes renewed, and thus kept the bank notes in circulation. There were certain evils inevitably associated with special charters, which, although much improved by laws applying to all banks alike, still existed under the safety-fund system in granting the charter, locating the bank, distributing the stock, and enforcing the provisions of the law.

GENERAL NOTE.—Where references are made to the Albany Argus during 1829 or before that date, the daily edition is meant. An abstract of the news from the daily was made in the semiweekly edition and the editorial columns dated by the daily editions. It is to these abstracts that reference is made under the date of the daily editions. In 1838 the regular daily edition is used. For all other years the date of the semiweekly edition on the outside cover is given.

^a Assem. Doc. 69, 1833, Vol. II, p. 8: Report of the Bank Commissioners.

CHAPTER II.

THE SAFETY-FUND LAW OF 1829.

The journals of the house for the session of 1829 show 29 petitions for the renewal of old bank charters and 37 for new banks and incorporations. The charters of these old banks were soon to expire. The senate committee reported in favor of renewals for all the old banks which had been fairly and honestly administered.^a This was the opportunity for the legislature to make any changes that seemed desirable in the system of banking.

It was at this time that Joshua Forman presented his plan to the governor for improving the banking system. Forman was a graduate of Union College, a public-spirited lawyer widely known, who had strongly advocated the Erie Canal project while a member of the legislature in 1808.^b His plan emphasized especially security for note issues. Because of their charters and the prohibition of private banking, the chartered banks had the exclusive privilege of furnishing a paper currency by which they made a profit. Therefore, the State should exact a guaranty for the soundness of that paper. The banks should in common be answerable for it.^c The idea was that all banks in the State should be formed into an association, so far as that all should be liable for the obligations of each, and yet allow the property

^a Sen. jol., 1829, p. 77.

^b *Encyclopædia of Contemporary Biography of New York State*, Vol. II. New York, 1882, pp. 277-280.

^c Assem. jol., 1829, pp. 179 et seq.

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and profits to belong to each in severalty. The plan was submitted to prominent New York and Albany bankers and approved in principle before it was presented to the governor. Forman and his friends hoped by this method to render it to the interest of each bank to sustain the credit of all other banks in the State.^a In presenting his plan, Forman advocated that banks be confined to discounting short-time commercial paper payable at maturity without renewal, and that they be compelled to invest their capital in safe public stocks or in bonds and mortgages. He asserted, what appeared to be the fact, that losses from the failure of banks, although considerable, were insignificant when compared with the public injury caused by the management of solvent banks. He had in mind the custom of banks of discounting and lending beyond the limit of safety and then suddenly calling their loans to meet obligations, to the ruin of many and the inconvenience of many more.

The governor, in his annual message, voices the public interest in the solvency of the banks and the stability of the paper, and urges the legislature to give its attention to these points in the banking system. He emphasized the objection, before made, that the severe measures adopted in 1827 might place banking in the hands of irresponsible men. He proceeded to outline the Forman plan, which was referred to the assembly committee for report. This committee prepared a bill on the lines suggested, which the chairman, Mr. Paige, presented to the assembly with a report in defense. This report

^a Cf. Hammond, Vol. II, pp. 297 et seq., for further details.

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maintained that the fundamental principle of banking was convertibility of paper into coin. One notices at once how completely banking was identified with note issue. Excessive issues must be guarded, and the committee recommended issue not to exceed twice the paid-up capital.^a The committee sought a plan which would avoid the objections urged against the principle of personal liability, and yet provide for the complete indemnity of the bill holder from all losses resulting from bank failure. The proposed plan seemed to them to secure the creditors of banks against every possible loss and to invite public confidence.

It was proposed to require each bank, for which a charter shall be granted, renewed or extended, to contribute a percentage of its capital to a common fund for the payment of all the debts of an insolvent bank, exclusive of the capital stock, after the assets of the bank itself had been exhausted. No bank could be required to pay more than one-half per cent on its capital yearly. These payments were to continue until 3 per cent of the capital had accumulated in the "bank fund," when the payments were to cease until the fund should be depleted by future payments. In case of such diminution of the fund the comptroller was authorized to call upon the solvent banks for additional contributions not to exceed one-half per cent in any year. The capital of the fund was to be invested in a specified manner, and after the expenses of administration had been paid the remainder of the income was to be paid to the banks

^a Paige report, Assem. jol., 1829, pp. 436 et seq.

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as dividends. It was provided that the affairs of the failed banks should be settled through receivers appointed by the court of chancery; and, upon order of the court, after the assets were exhausted, the comptroller was authorized to pay the debts still unpaid, exclusive of the capital stock, out of the fund.

Three bank commissioners were provided for—one appointed by the governor and two by the banks—whose duties were to visit each of the banks organized under the law at least quarterly, and oftener if requested by three safety-fund banks. They had power to examine the officers under oath and to investigate the affairs of the bank thoroughly enough to determine, if possible, its solvency. If the bank was found to be violating the provisions of its charter or of the safety-fund law, it was provided that the commissioners might apply for an injunction against the bank, and if the investigation satisfied the court that such a course was necessary, a receiver could be appointed to close the affairs of the bank. It was provided in section 28 that the corporation might be dissolved if it should neglect its payments to the fund, if it should lose half its capital, if it should suspend specie payment for ninety days, or if it should refuse to be examined.

The banks were required to report under oath annually to the commissioners, who were directed to prepare an abstract of the returns and submit it to the legislature with their annual report. Their term of office was to be two years, and they were removable by the governor.

The issue of bank notes was restricted to twice the paid-up capital and the loans and discounts to two and one-

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half times the capital. The penalty for a false statement by officers, or for the exhibition of false papers with intent to deceive the examiners, or for false entries in the bank books was imprisonment for from three to ten years. The act modified the Revised Statutes of 1827 as to the liability of stockholders, as before explained. They were no longer personally liable. This was again modified in the constitution of 1846 so as to hold them responsible, as at present, for an amount equal to the amount of their stock paid in. The commissioners were prohibited from being stockholders in any bank. The rate of interest was regulated. The capital stock must all be paid in and an oath of the officers to this effect filed before opening the bank for business. This was a great advance over the previous system of allowing part of the capital to remain unpaid, and thus offering the temptation to all the evils which we have described in connection with banking on the notes of stockholders or on an utterly inadequate cash basis. Such was the law proposed and finally passed after warm debate.^a

In order to learn the attitude toward this proposal, it will be worth while to follow the debates on the bill briefly. The committee which presented the bill predicted that the new system would impart stability and currency to the circulating medium, prevent runs on banks, and avoid combinations between institutions to destroy a particular bank. The city banks had been accused of trying to ruin certain country banks, but under the proposed plan each would be interested in upholding the others.

^a For text of act cf. Assem. jol., 1829, pp. 752-756, or Laws of 1829, chap. 94.

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To objections against the bank commissioners the committee asserted that it was not a new principle and was meant to ascertain whether the high trust of creating a currency was being properly executed. Such inspection would be desirable for the stockholders because it would increase the confidence of the community in the bank's paper. Merely powers of inspection were granted, and therefore the commissioners could not seriously injure any particular bank by the exercise of their powers. To the court was granted the final decision as to a permanent injunction. The banks would be benefited because there would be a set of men whose express duty it would be to prevent insolvency and losses which the banks themselves would have to pay.^a No solvent bank could be required to pay more than one-half per cent annually on its capital, and in some of the States there was a 1 per cent tax annually on banking capital.

The speaker of the assembly argued that the fund was inadequate, as indeed it proved, for all the debts of the banks. He pointed out that the banks were permitted to issue notes far beyond their capital and that in case of serious failures settlement from the fund might be delayed over four or five years, which proved to be the case later. Meanwhile the farmer and the mechanic must wait and suffer loss. He considered the Revised Statutes preferable to such a law.^b A few days later the speaker offered a substitute for section 2 of the original bill creating a fund, in which he advocated the usual tax on banks, but

^a Paige rept., Assem. jol., 1829, pp. 439-440.

^b Albany Argus Feb. 28, 1829. Report of debate in the House Feb. 27, 1829, on safety-fund bill.

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the tax to be allowed to accumulate up to \$5,000,000 as a bank fund from which the bills of failed banks might be paid. The fund would be kept at that amount, and whenever it exceeded the amount the tax on banks would be used for general expenses as before. In case of a bank failure the legislature may provide by special act for the payment of the bills out of the fund. In this substitute the notes of a failed bank alone were secured by the fund, and not all its debts. This seems to have excited no comment. It indicates how completely the legislature was concerned in securing the note holder by the new law. Losses by depositors were not mentioned.^a Objection was of course made to the speaker's substitute on the ground of delay in redemption and consequent losses.

Another representative, Mr. Hubbell, pointed out that the very existence of such a fund would relax "public scrutiny and watchfulness which now serve to restrain or detect misconduct."^b This argument appealed to many then, and to-day, when deposits have assumed such a large place in the modern banking business and when a bank extends its credit not only by bank notes but much more by deposit accounts, the argument assumes added weight. Mr. Dickson objected also to the fund idea because it required a "compulsory partnership" between institutions which knew nothing of each other. It was, moreover, morally wrong to transfer losses from bill holders, or the community generally, to the stockholders, who might be equally innocent of any wrongdoing in the failure and unable to bear the responsibility. The fear

^a Albany Argus, Mar. 4, 1829. Debate in assembly on bank bill, Mar. 3,

^b Albany Argus, Feb. 28, 1829.

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was also expressed that a monopoly would be formed, a "monied aristocracy," which would control future applications for bank charters or combine to crush individual banks.^a The multiplication of banks and the increase of competition might enlarge the bank fund but it would also decrease the profits of existing banks. This attitude had been very early shown by the chartered banks.

The argument grew spirited between those, on the one hand, who thought the Revised Statutes on banking were "odious fetters" and that they would prevent men who were financially responsible from venturing into the banking business, and on the other, those who objected to their repeal, except perhaps the clause requiring directors to repel by proof the presumption of fraud, on the ground that these requirements were the only defense against fraud and complete control by the agents and officers of the banks. Many were sure that the "bank fund" would put a premium on reckless banking and encourage the unscrupulous to put in circulation all the bills possible, and, since the notes were secured by the entire banking capital of the State, it was maintained that this would be easier to accomplish because those who took the notes would be less watchful and exacting. It was pointed out that the bill holder was guarded, but not the stockholder. Many were skeptical of the power of commissioners to prevent fraud and insolvency because, it was said, they must depend upon the statements of bank officers anyway and would prove no more efficient than the reports already required.^b Besides, it was feared that their

^a New York Evening Post, Mar. 4, 1829.

^b New York Evening Post, Mar. 28, 1829.

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duties were "inquisitorial" and that such power might be used to ruin individuals.

Notwithstanding the fact that Mr. Forman had presented his plan for approval to several city bankers and financiers, there developed a very serious opposition from the New York City banks. This will be explained by references to the table showing the items of the statements of city and country banks, presented for 1828, in the last chapter. It was there pointed out that the capital and deposits of the city banks were much larger than those of the country banks and that their use of notes was much more restricted. Although the safety-fund law allowed the issue of notes to twice the paid-up capital, the table, referred to above, shows that the city banks kept in circulation less than one-third the amount of their capital. It was quite different with the country banks, which circulated notes far in excess of their capital. Now, the chief fear, as shown by all the legislative debates of this and other legislatures, was for the security of the current bank notes. The law of 1829 proposed to levy the assessment for the fund upon the capital of the banks, not upon the amount of notes issued. Losses from other sources, while secured by the fund, were not emphasized in the debates. Therefore, the city banks objected to a tax upon their large capitals to support a fund to secure not only their own notes, which were small in amount compared with their capital, but also the notes of the country banks, which were issued to amounts much larger than their capitals, upon which the same assessment was made. The fund was not liable for the capital stock. Besides, such a law, they alleged, would make them partners of

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the country banks and would reduce their credit to the same level.

The final vote on the bill in the house stood 76 to 29 and in the senate 20 to 6. Of the delegation of 11 in the house from New York city and county, 5 voted for the bill and 4 against, with 2 not voting. In the senate 3 of the 6 negative votes came from the first district, of which New York City formed a part.^a

It is interesting to note here that in the assembly, before the bill passed, Mr. Mann offered a proposition that all bank notes be countersigned by a central agent and issued to the banks in authorized amounts in order to prevent fraudulent overissues and counterfeiting. The amendment was not adopted, and in consequence the bank fund was charged later with a large amount of illegally issued notes.^b This defect was not remedied until 1843, when the solvent banks had actually suffered at the hands of unscrupulous bankers.

By the new law stockholders were relieved from personal liability imposed in the Revised Statutes, but the responsibility of directors to the stockholders was retained as provided in those statutes. It must not be forgotten that the restrictions before described as to the payment of all the capital before opening and an oath to that effect by the officers were retained. This oath must also state that no loans had been made to enable a stockholder to pay his stock and then receive a discount from the bank to discharge the debt. The other provisions of

^a Assem. jol., 1829, p. 757; also Sen. jol., 1829, p. 393.

^b New York Evening Post, Mar. 19, 1829.

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the Revised Statutes stated in Chapter I, except as modified by the safety-fund law of 1829, remained in force.

At the session of 1829 16 old banks were rechartered and 11 new ones.^a The provisions of the charters were uniform. They specified the place of deposit and discount, the duration of the charter, amount of capital, precise powers in addition to the general powers granted in the Revised Statutes, chapter 18, the restrictions as to capital, notes, and loans and discounts, the provisions for contributions of one-half per cent annually to the bank fund, and for inspection by the commissioners.

The New York City banks refused at first to accept charters under the new law. It was pointed out that the city banks paid lower dividends than the country banks and could not charge as high an interest rate, because of the competition of the United States bank. Therefore they could not afford the added one-half per cent tax for the fund. Editorials in the *Evening Post* predicted ruin for the city banks under such a law.^b Mr. Paige, in the assembly, in a debate on renewing the charter of the Mohawk Bank, at Schenectady, admitted that the law was not as favorable to the city banks as to the country banks; but the act was the best that could be adopted in the state of variant opinions.^c Dickson, in debate on a bill to extend the charter of the Union Bank of New York City, declared some concessions to the New York banks were "just and reasonable," since the law operated more

^a Albany Argus, May 6, 1829. Verified from legislative acts.

^b New York Evening Post, Apr. 1 and 3, 1829; Albany Argus, Apr. 6, 1829.

^c Albany Argus, Apr. 9 and 17, 1829.

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severely against them. He said that he had favored the safety-fund plan because he thought it would be "likely to reconcile conflicting opinions and as decidedly preferable to the then existing system." He pointed out that for years the dividends of city banks had averaged about $5\frac{1}{2}$ per cent, and to deduct one-half per cent from this might cause the withdrawal of many stockholders. He attributed the smaller dividends of city banks to less use of bank notes and their quick return for redemption, as well as to greater expense of operation. More specie must be kept also to meet foreign demands.

Soon after the law was enacted the Middle District and Columbia banks failed. These two failures gave the New York City papers an opportunity to find fault with the new bank law, the "country banks," and the country members of the legislature. One of the city papers declared that it would be very convenient to have the coffers of the city banks responsible for the defalcation of those in the country, and now it was possible to understand the anxiety of the country members for the passage of the safety-fund act.^a Really these failures were an argument in favor of the new law, for they were incidents of the old system, not chargeable to the new.

The governor, in his message in 1830, stated that the provisions of the law had received the decided approbation of the public, but reported opposition from the banks as to the severity of the Revised Statutes in reference to the responsibility of directors to stock-

^a Albany Argus, June 1, 1829.

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holders. He was of the opinion that these restrictions might be modified under the safety-fund system.^a The legislature, as explained in Chapter I, proceeded to repeal sections 11-18, inclusive, of the Revised Statutes, which relieved the directors of banks incorporated in the future from liability except for amounts involved in specific provisions in sections 1-9, described in Chapter I.

Besides the 27 banks chartered or rechartered under the new law in 1829, 9 new banks were authorized in 1830; 8 were rechartered, all in New York City, and 9 were chartered for the first time in 1831; 2 were rechartered and 7 were chartered in 1832, and from 1833 to 1836, inclusive, 28 new banks were authorized. In 1836 the capital of the Dutchess County Bank was increased and the bank placed under the safety-fund law. In 1839 two banks were rechartered under the safety-fund law. This is a total of 93 banks, either chartered or rechartered under the law of 1829. There were never more than 91 in actual operation at one time.^b

The debates on the safety-fund law, as before pointed out, made little reference to security for other debts of a bank than note issues. The country banks made their loans chiefly from capital and their own notes, and the latter exceeded the former in the small banks. The bank commissioners pointed out in their report to the legislature, in 1834, that in the United States the issues of paper "depend almost entirely upon individual

^a Sen. jol., 1830, p. 22.

^b Root: Sound Currency, Vol. II, No. 5, pp. 6, 7; also table giving names, location, capital, etc.

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discounts, regulated in amount by what the banks consider their ability to redeem."^a Every note discounted made a new emission of currency. No special effort was made by the new system to protect the stockholders of a bank, the chief concern being naturally the note holder. The fund was not liable for the capital stock of a bank. This would not be so true of the city banks where the deposit business had developed to a considerable extent. Most secondary writers on the safety fund refer to this guaranty of all the debts of a failed bank as one of the chief defects of the system. The makers of the law themselves did not apparently realize the significance of the guaranty until the bank failures of 1840-1842 caused the system to break down under the burden, and mortgaged the fund for the rest of its existence. The commissioners, in their report in 1841, declared that all debts, exclusive of capital, were a charge upon the safety fund. This feature, they declared, "does not, until recently, seem to have been generally understood, either by the public at large or even by those engaged in the business of banking."^b The report goes on to express doubt of its justice or expediency and asserts that the law of 1829 was "primarily designed to secure bank-note holders and not depositors or other creditors."

The free banking system under a general law was inaugurated in 1838 and no more special bank charters were granted by the legislature. Under this system securities must be deposited for the full value of the notes issued,

^a Assem. Doc. 102, 1834, Vol. II, p. 10.

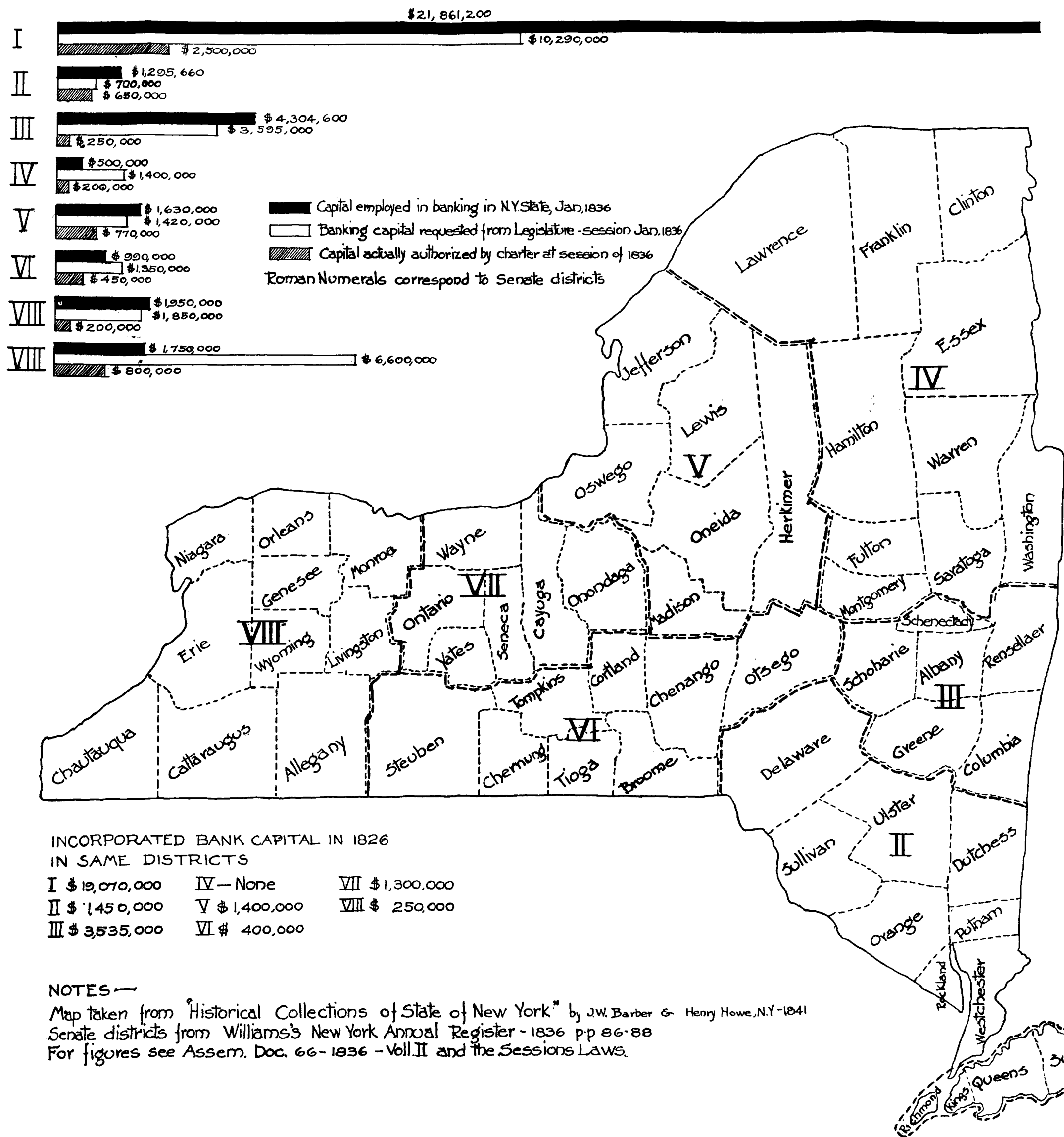
^b Assem. Doc. 64, 1841, Vol. III, p. 16.

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as at present under our national banking law. No guaranty was attempted for the other debts of a bank. The Canadian system likewise furnishes a guaranty for notes only, by providing a fund of 5 per cent of the average circulation from which the notes of failed banks are redeemed.

Having studied the banking conditions antecedent to the safety-fund system, and having seen the new system in operation, we will now turn to a study of the banking experience under the plan of the safety-fund law.

BANKING CAPITAL IN NEW YORK IN 1836



INCORPORATED BANK CAPITAL IN 1826 IN SAME DISTRICTS

I \$19,010,000	IV—None	VII \$1,300,000
II \$1,450,000	V \$1,400,000	VIII \$250,000
III \$3,535,000	VI \$400,000	

NOTES —

Map taken from "Historical Collections of State of New York" by J.W. Barber & Henry Howe, N.Y. 1841
Senate districts from Williams's New York Annual Register - 1836 pp 86-88
For figures see Assem. Doc. 66-1836 - Vol. II and the Sessions Laws.

CHAPTER III.

THE TEST OF THE SAFETY-FUND SYSTEM.

I. OPERATION OF THE SYSTEM BEFORE 1840 WHEN SERIOUS FAILURES BEGAN.

In January, 1832, the bank commissioners reported that capital invested in safety-fund banks had increased from \$6,294,600, at the time of the last report, to \$18,856,800. Circulation of notes of banks outside of New York City had largely increased, partly owing to the use of the capital of the canal fund which, as invested, "may be considered as an addition to the bank capital of the State."^a There was buying of the stock of new banks for speculation, since especially the country banks yielded above the legal rate in dividends. The report gave warning of the danger of overissue and too much bank capital. The large banks, however, particularly the city banks, are restrained in their issues by the rapidity of the return of their notes for redemption and the wider use of the check system.

The report of the commissioners in January, 1833, calls attention to the small specie reserve, less than \$2,000,000, to support a circulation of \$12,000,000 in notes, and warns the legislature of the danger in times of panic and depression. It is pointed out also that the legitimate function of banks is not the loaning of capital, but to furnish a sound currency.^b What the report really does is to distinguish between the bank of issue and the bank

^a Assem. Doc. 70, 1832, Vol. II, p. 7.

^b Assem. Doc. 69, 1833, Vol. II, p. 5.

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of deposit and discount. Capital for industry should be borrowed from individuals or corporations not associated with the business of circulation, for the bank of issue, in order to sustain its circulation, must make loans for short periods. The report goes on to assert that "of the discounted paper of the country banks we should think less than half was entitled to the denomination of business paper;" that is, paper founded on actual business transactions to be paid at maturity.^a Much paper discounted was evidently made to procure a loan, and often renewed. This was accommodation paper and might be called in by the bank suddenly or a renewal might be refused at a critical time when the borrower most needed help, especially if the redemption of bank notes was demanded with unusual frequency.

The report of the following year again urges that the amount of the currency should be proportioned to the amount of business, and should not be enlarged to furnish capital to create business.^b Experience had so far indicated that the establishment of new banks in the country increased the aggregate circulation by about the amount of new capital created,^c without a corresponding increase in the specie reserve. The demand for new banks was growing, but the commissioners recommended the increase of the capital of old banks rather than the creation of new ones, on the ground that this plan would furnish the most capital to the community with the least addition to the circulation. The average circulation for a bank with

^a Assem. Doc. 69, 1833, Vol. II, p. 8.

^b Assem. Doc. 102, 1834, Vol. II, pp. 10 et seq.

^c *Ibid.*, p. 14.

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\$100,000 capital was about \$160,000, but for a \$300,000 bank the circulation seldom exceeded the capital. Therefore the security of the larger bank was greater, for the claims of the public for notes were proportionately less upon it.

The report in January, 1835, gave the description of a severe pressure in the money market, when all the branches of industry seemed to be in an unusually prosperous condition. It was called a political panic. Uncertainty was made to pervade the public mind. The banks were attacked; charges of insolvency were circulated; the people were urged to demand specie, and it was predicted "that the safety fund was crumbling to ruin."^a

Banks in the country were not then required to redeem their notes except at their counters. They did not, however, depend on specie in their vaults, but kept funds in the city banks, where they accumulated in the natural course of business, and redeemed their paper by drafts on the city. This redemption was interrupted in 1834, according to the commissioner's report, not because the country banks were unable to redeem, but because the city banks stopped taking up their notes and sending them home. This led to charges injurious to the country banks. As proof that they were able to redeem their paper when sent home, the country banks did later take up within sixty days \$2,000,000 of their circulation.^b Public confidence was not seriously impaired, thanks, as the commissioners pointed out, to the safety-fund law.

^a Assem. Doc. 74, 1835, Vol. II, pp. 5 et seq.

^b Ibid., p. 7.

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The report again asserted that the amount of specie was too small for proper security when the banking capital and note circulation were so rapidly increasing. It was proposed to prohibit smaller denominations of notes and limit the circulation to the amount of the capital instead of twice the capital, as at present. To suppress small notes would infuse more specie into the circulation. The average dividends of all banks for the past three years was reported as 7.31 per cent, and the dividends of country banks, which would be most affected by the suppression of small notes, were considerably higher than the city banks. Therefore the banks could bear the changes proposed. At the same session at which the above report was rendered the legislature passed a law forbidding the circulation of bills under \$5 after a specified time. The measure was unpopular and became a political issue in the next campaign for governor. The law had to be modified in 1837 when specie payments were suspended.^a

The report of the commissioners called attention to the practice of stockholders of borrowing capital with which to pay their stock. In some instances the stock of the bank was pledged as security in the hands of those from whom the capital was borrowed. This was a dangerous practice, because under pressure the stockholders came to the newly opened bank for an accommodation loan, and the operation became equivalent to withdrawing the capital just paid in by substitution of the notes of the stockholders. The commissioners recommended that char-

^a John Jay Knox: *History of Banking in the United States*, 1900, pp. 407-8.

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ters granted in the future have a provision prohibiting the hypothecation of the bank stock for at least a year after the opening of the bank.^a The report in January, 1836, urged again that the legislature require money paid on capital stock of new banks to be raised by the individuals without pledging the stock itself.^b The pressure for new banks was very strong and speculation had become a mania. Bank stock was a profitable investment and many were eager to get it only to sell it again at a premium. Consequently they borrowed capital for dealings of this character and sometimes exploited the bank in paying back their loans.

During the session of 1835 the banks were investigated by the bank committee of the assembly with reference to certain practices referred to in the governor's message of that year. The governor said, "Instead of discounting notes according to the usual course of business they (the banks) have required drafts of their customers, payable at some distant place, knowing that the drawers had not and did not expect to have funds at such place to pay them; when these drafts arrived at maturity, others were offered to the same banks and taken in payment of the former. A discount of 1 per cent beyond the legal rate of interest has been exacted on these successive drafts."^c The charge was made that this was a method of securing more than the legal rate of interest from those who were under the necessity of seeking accommodations from the banks. It was a method of

^a Assem. Doc. 74, 1835, Vol. II, p. 24.

^b Assem. Doc. 80, 1836, Vol. II, p. 15 et seq.

^c Assem. Doc. 229, 1835, Vol. III, p. 4 et seq.

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increasing the profits of the banks who practiced it, in a manner similar to those banks which, being organized primarily to circulate notes, established offices at some distant place, difficult of access, and then redeemed the notes issued, not at their counters, but at offices in the city, where they charged a discount and thus made profit. The bank commissioners had referred to the practice of giving preference to discount of paper payable in the cities, especially by some banks in the western part of the State, and then charging the premium of exchange on its renewal. It was natural and proper for banks to prefer paper payable in the cities when based upon actual business operations, "but to compel or encourage the making of such paper for the mere purpose of being able to exact a premium * * * can be nothing less than an evasion of the law and, in many cases, grossly oppressive upon the borrower."^a The offense here referred to seems to have been the discount of accommodation paper, and as a condition, expressed or implied, requiring it to be made payable at Albany or New York, on which, at maturity, the bank could charge the premium of exchange in addition to the discount on the renewal paper. The committee found some evidence of this practice. The great difference in rates of premium charged on drafts by different banks in places very similarly located is irreconcilable with the idea of a "fair sale of drafts for purposes of remission."^b The committee warned the banks that such practices would draw public

^a Assem. Doc. 229, 1835, Vol. III, pp. 4-5.

^b *Ibid.*, p. 10. See figures showing these differences.

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suspicion and censure upon banks generally in the interior of the State. The committee commended the preference of paper payable in the city, if done in good faith, and characterized the sale of drafts upon the city at a fair premium as just and economical. Banks must not be condemned indiscriminately; but where they make the motive for giving a discount the hope of selling a draft at a premium to pay it, they should be censured. At the session of 1835 a law was passed which was designed to remedy the above evil. It prohibited a bank from receiving premium of exchange on any draft made by the bank, used or applied in payment of any bill, note, or other demand, due to or discounted by said bank. It was also made illegal for any bank to place money or notes in the hands of any person for the purpose of loaning or discounting. It had been complained that some banks did this to the profit of their officers.^a

No bank charters were granted in 1835. The report of the commissioners in January, 1836, had a distinct note of warning. The circulation and deposits were greatly increased, and the discounts had grown by almost \$7,000,000. There had been an increase of specie, due largely to the recent law suppressing small notes, which operated well and was approved. The demand for new banks at the session of 1836 was stronger than ever. There had been a large investment of capital in western stocks and real estate, which increased the pressure on the banks for ordinary business. The "mania of specu-

^a Laws of 1835, chap. 307; also John Cleaveland: *The Banking System of the State of New York*, 1864, pp. 77-79.

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lation" was growing. Caution was urged in increasing the number of banks. It was recommended rather to increase the capitals of the old ones because by this method the currency would not be expanded to such an extent. "By connecting the currency with the success of such enterprises (speculations), we should not only give fresh impulse to the excitement, but expose the whole community to the disastrous consequences of a revulsion."^a Some banking capital was required, but in no proportion to the amount asked for.

The governor, in his message in 1836, said that already notices had been published of intended applications for 93 new banks during the session.^b He warned the legislature against supporting the growing speculative movement and urged provision for the stability of banks in times of panic. He called attention to the destructive cycle of overtrading, expansion of credit, overissues of paper, speculations, reactions, contraction of paper, dull trade, and bankruptcy.

A reference to the map at the beginning of Chapter III will show graphically how large was the capital employed in banking previous to this session of 1836, and how it was distributed over the various senatorial districts of the State. It will also be evident how immense was the increase demanded from the legislature during this single session of 1836, as well as the small amount granted by the legislature compared with that demanded. It appears from this map that the capital had been, in general, distributed over the State by the legislature in about the

^a Assem. Doc. 80, 1836, Vol. II, p. 11 et seq.

^b Semiweekly Albany Argus, Jan. 5, 1836.

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proportions which the various districts would naturally need. Most was needed in the First district, where New York City was located, and the next district in importance was naturally the Third, in which the state capital was situated; the Second was overshadowed by the New York City banks, and the Fourth was comparatively undeveloped. The Fifth, Sixth, Seventh, and Eighth districts were rapidly developing and each had about the same amount of banking capital. In 1836 the Fourth, Sixth, and Eighth asked for much more than they had already employed. Especially in the case of the last district, this was probably to be explained on the ground that it was the farthest west and most subject to the boom in real-estate speculation. Banking capital was desired to aid in this wild rush for wealth. It will be noted, however, that the legislature was conservative in granting only a very small percentage of the amount requested. New York City was probably largely influenced to demand a large increase because the United States bank was closing up its affairs. In both the First and Third a relatively small increase was granted.

By comparing, from the map, the amount of incorporated banking capital in 1826 with that in 1836, in the same districts, we can not say that there had been, under the safety-fund system, an extravagant increase in banking capital. Of course, under the safety-fund law all the capital authorized must be paid in and actually employed, which was not true under the previous system.

The legislature of 1836 passed an unusually large number of laws, few of a public nature. It chartered 12 new banks out of the large number of applications, and in-

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creased the capital of two old banks. The aggregate capital added was \$5,670,000.^a The charters passed the house by votes ranging from 96 to 24, to 88 to 29.^b The votes in the senate were all by such majorities as 24 to 3 and 22 to 6.^c Therefore, it can not be claimed that these charters were passed by a very close vote. They required, of course, a two-thirds vote. An article in the Albany Semiweekly Argus, April 25, 1837, entitled "The Times," refers to these bank charters and the plan of securing the capital to purchase the stock, in some cases. It was asserted that the funds were advanced by trust companies and other banks to persons wishing to buy stock. These persons, in some cases, received discounts from the new bank to pay these debts. This was substantially the old stock-note system. A resort to this method shows that stock was sought for speculative purposes and that there was little real capital to be employed in banking. When we consider that 5 of these 12 banks chartered in 1836 failed before the close of 1842, these facts assume grave importance.

The bank commissioners' report, in January, 1837, stated that the distribution of the stock of new banks was the cause of "violent contentions and bitter personal animosities."^d This was done, as explained in Chapter I, through commissioners appointed by the legislature

^a This counts the Dutchess County Bank increase of capital to \$450,000. By the reports of the bank commissioners it was increased to \$600,000, making the total increase \$5,820,000. For \$5,670,000, see *Semiweekly Argus*, May 31, 1836.

^b See *Semiweekly Argus*, May 31, 1836, for these and other votes.

^c See *Semiweekly Argus*, May 17, 1836.

^d *Assem. Doc.* 78, 1837, Vol. II, pp. 7 et seq.

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from the neighborhood of the new bank. The distribution was sometimes made a part of the spoils of the victorious political party and sometimes a matter of profit to the commissioners and their friends. Thus the stock and, consequently, the control of the bank sometimes fell into the hands of those least qualified in character or financial responsibility.

The governor, in his message in 1837, urges a different method of distribution of stock.^a Mr. Young, in a debate in the senate in 1837, referred to the last session when so many senators aided in passing bank bills and then went home to share in the profits of the stock. A resolution was introduced calling for the investigation of the conduct of a senator who sold bank stock at a great advance. Much bitter feeling was aroused and many accusations were made.^b A general resolution was later introduced and debated hotly—

“Resolved, That, in the judgment of this senate, it is highly improper for a member of the legislature to vote for the passage of a law creating a bank or moneyed corporation, and afterwards to solicit or receive stock in said corporation on the distribution of the stock thereof.”^c

At the session of 1836, the capital of the Jefferson County Bank was increased. The manner in which the additional stock was distributed was a matter of investigation by the next legislature. It was found that the nine commissioners had opened the books for subscription August 15, 1836, and had kept them open through

^a Semiweekly Argus, Jan. 10, 1837

^b Semiweekly Argus, Jan. 20, 1837.

^c Semiweekly Argus, Feb. 3, 1837.

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the following day. About 500 persons applied for stock, which oversubscribed the amount. The commissioners met to distribute the stock. There were two parties among the commissioners, and each party made up its own list of favored applicants for stock. The party that numbered five carried its list and really distributed the stock. One of the majority party asserted that they calculated "to have the stock where we can lay our hands on it." Before the distribution, Lowery Barney received from several persons power of attorney to subscribe for stock in their name. He generally took the persons' notes for the amounts to be paid on their subscriptions, which amounts he paid at the time of subscription. All those persons who gave power of attorney received stock, while many other subscribers were refused. They soon transferred their stock to Barney, who sold it to G. C. Sherman, the man who really furnished the money with which to buy the stock. Barney was the agent of Sherman. Others did the same thing in order to acquire more stock than was allowed under the act of incorporation. These persons were shown to have borrowed large sums to enable them to carry out these operations and pay up their capital stock. The largest stockholders were indebted for stock purchased, on notes not payable until after the election of directors. The investigation showed that \$45,400 of stock had, since the original distribution and previous to the payment of the last installment, been transferred by various persons to G. C. Sherman; \$10,550 to Alphius Green, and \$7,200 to L. Paddock. These three received in the original distribution the full amount of stock allowed by law. Out of

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about 500 original subscribers, 97 actually received stock in the first distribution. Every one of the 9 commissioners received the maximum amount allowed by law, 250 shares. At the time the committee investigated, after the above transfers of stock had taken place, there were only 36 holders of stock, an average of 333 shares, but 7 men held 7,695 shares of the whole 12,000 which was originally placed in the hands of 97 persons. Truly, they had placed it where they could lay their hands upon it. The committee decided that the distribution was illegal and improper—partial and unjust. It appeared clear that there was an understanding between the commissioners and others to give certain persons more than the law allowed.^a

At the same session another case was investigated, this time by a select committee of the senate. It was found that the same methods were used in the case of the Oneida Bank that have been detailed for the Jefferson Bank. Some of the commissioners themselves were instrumental in procuring authority to subscribe for stock, the power to sell the same afterwards, and a blank form of hypothecation of the stock so subscribed as security for moneys advanced to pay the subscriptions. By this means large blocks of stock came into the hands of a few persons. In several cases three of the commissioners advanced the funds for the subscribers who gave them authority to subscribe stock for them. The maximum allowed by law in this case was 25 shares of stock. The reason assigned for the above operations by three of the commissioners was

^a Assem. Doc. 284, 1837, Vol. III, for above details.

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“to secure to themselves and their friends the control of the said bank.” The committee condemned such conduct as incompatible with “pure, fair, impartial, and discreet exercise of their duties.” It was shown that the bank’s stock, to the amount of 1,076 shares, or \$106,350, had been hypothecated to the Farmers’ Loan and Trust Company on November 8, 1836, by 14 different persons, all to raise money to pay the subscriptions due on the bank stock.^a

The concrete cases just explained will make clear the purpose of an act passed in 1837 to remedy the evils of stock distribution. It provided for the sale of the stock at public auction, with three weeks’ notice of the time and place. The size of the shares was regulated at \$100. On the first day of the sale the commissioners must not sell more than five shares to any one person. If the sale continued the second day, they must not sell more than 10 shares to one person, and on the third day, if the sale continued, not more than 20 shares to one person. A person, to purchase stock on the first three days of the sale, must be a resident of the county where the bank was located. The purchaser must not sell, assign, transfer, or pledge in any manner his stock until at least three months after the whole capital was paid. Before the payment of the last installment on the stock or within twenty days afterwards, each stockholder must take oath that he is the *bona-fide* holder of the stock purchased by him and has paid for it with his own money; that it is not pledged or hypothecated at all; that he had not contracted to sell or pledge it, and that he owns no other stock in the bank, directly or indi-

^a Sen. Doc. 58, 1837, Vol. II, for above details.

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rectly. False swearing was subject to penalty for perjury in the above cases.^a When the evils of distribution were remedied it was too late, for no more charters were granted for new banks under the safety-fund system.

The session of 1837 was characterized by bank investigations. In January a resolution was introduced into the assembly requesting a select committee to inquire whether the banks had been guilty of illegal or improper practices, contrary to the letter or spirit of their charters—i. e., application of their funds to other purposes than legitimate banking, usury, speculation, etc. Other similar resolutions were offered.^b In February a petition of citizens of Alleghany County requested an investigation of the banks, fearing “the presence of a licensed aristocracy in this county.”^c The petitioners made charges of oppression and opposed the present system of banking on the ground that it promoted speculation, impaired men’s morals, granted a monopoly power to a few, made it possible for banks to refuse loans to business men and small dealers, and endangered the welfare of society. A select committee reported that the Sacketts Harbor Bank had violated the law as to circulation of paper as money and its charter was promptly repealed.^d

A select committee reported on the safety-fund banks, having for its object to discover whether the evils reported were inherent in the system itself or whether they

^a *Semiweekly Argus*, May 23, 1837, for above text.

^b *Assem. Docs.* 34 and 42, 1837, Vol. I; and *Assem. Doc.* 130, 1837, Vol. II.

^c *Assem. Doc.* 130, 1837, Vol. II.

^d *Assem. Doc.* 243, 1837, Vol. III.

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are such as may occur under any system. "If the officers and conductors of the banks have perverted the privileges and immunities of the institutions to purposes of fraud and oppression, they should be held amenable."^a The report went on to state: "Nothing has been discovered in our banking institutions generally which should tend to the destruction of confidence in them. * * * Your committee are of the opinion that many of the abuses which have been charged and may have been practiced are not attributable to the system by which they were created, but are alone chargeable to the cupidity and avarice of those who have been intrusted with their management."^b The committee investigated specific charges and made inquiries of all the safety-fund banks. In the report the details and evidences are given for each bank. We shall not review the charges, which were not substantiated by the committee, but only the practices actually found and proven by the committee. Of the latter we shall give a brief summary, and that not for individual banks. It was found that many of the charges against New York City banks were not supported by good evidence. Some banks had extended their loans even beyond limits of prudence. Some loans to individuals seemed too large in comparison with the capital, but these were explained by the officers as temporary and in process of reduction. Some of the city banks were making large temporary loans, subject to call, which the officers asserted to be necessary in order to meet the large government drafts without suddenly curtailing discounts. It will be

^a Assem. Doc. 328, 1837, Vol. IV, pp. 4 et seq.

^b *Ibid.*, p. 6.

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remembered that the Government was distributing its revenues among the States. Most of the customs dues were collected in New York City. Therefore, there was a constant draft on the city banks by the Government to remove its funds. The temporary loans were made on stock hypothecated as security. The committee recognized that, in most cases, the motives for these loans were good, but also asserted that it had become a cause of clamor against the city banks, because it enabled brokers and others to secure funds with which to speculate, in buying up the paper of banks at a discount. The committee therefore recommended that no bank be allowed to take stocks in hypothecation, because it regarded the practice as a leading cause of difficulty in the city banks. Of course banks were already prohibited from taking their own stock in hypothecation. This idea of the committee, both as to the expediency of temporary loans and the hypothecation of stock as security, would not meet with much attention to-day when it is generally recognized that the loans of a commercial bank must be liquid and can best be made so by short-time loans on good business paper and by call loans to those who need funds temporarily. Stocks to-day form a large part of the collateral offered for these short loans. In 1837 it was a question of what stocks were good collateral and what sort of loans might wisely be made. Banking experience has developed far since then, but the same problems arise. Then, the opposition evidently arose because of the operations of speculators in bank paper whose business was encouraged by some banks through temporary loans. Further, these

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loans sometimes endangered the solvency of the bank when the security depreciated in value or proved worthless. But the same thing may happen to-day, although, in general, our information about stocks is more accurate now. It was taking a more serious risk for banks to accept stocks as security in 1837.

Among some of the country banks it was found that loans to individuals were in amount out of proportion to capital. "The committee are of the opinion that a bank can never be either so safe and profitable to the stockholders, or so useful to the community, as when its discounts are confined to legitimate business paper, the discounts of moderate amounts, and of course extensively diffused."^a By large loans to the few, many were excluded from accommodations, and the jealousy of the public was aroused. If, as in some cases, these loans were confined to the officers and directors, then indignation and distrust were invited.

The officers of several of the banks were found to be purchasing paper at a discount, in some cases apparently with their own funds independent of the bank, but in other cases, after the paper had been refused for discount at the bank, and with funds which they secured in large amounts from the bank. This practice was calculated to excite public odium and discredit the bank. In other cases the bank loaned to brokers who made a business of buying notes at a discount. This made the bank a sort of broker's office. Such discounts by officers of banks and by brokers were usually at high rates and were there-

^aAssem. Doc. 328, 1837, Vol. IV, pp. 36-37.

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fore, when previously refused at the bank, a species of usury by the bank and actuated by greed on the part of the bank's officers. It was discovered that in most cases the officers, when in this business, borrowed heavily from the bank, even when they testified that they were doing the discounting with their own private funds. Such loans to officers were apt to be poorly secured. Banks themselves were sometimes guilty of usurious practices, as shown by the investigation in 1835, before described, when they discounted paper, and as a condition of the discount required that it be made payable in New York or Albany, in order to be able to sell drafts for the proceeds and charge, in addition to the discount, a premium of exchange. The Bank of Orleans was a great offender in this sort of transactions. The directors intrusted the affairs of the bank to the cashier who abused their confidence. He refused discounts at the bank and then purchased the notes "for his own account at the bank, and with the funds of the bank, at a usurious and ruinous rate of interest." He allowed two clerks to overdraw to the amount of \$20,000, which they used to purchase notes at 3 per cent per month offered to the bank for discount and refused. Three of the directors were guilty of the same practice. In 1837 the bank commissioners discovered these practices and took measures to close the bank, but immediate reforms were begun and the cashier resigned, so that the bank was allowed to continue. This shows the wisdom of bank examinations.^a Too little care

^a Assem. Doc. 256, 1838, Vol. V, for details.

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was shown by stockholders in electing directors, or by the bad system of distributing stock the bank was allowed to fall into the hands of speculators or unscrupulous men. Proxies were sometimes secured in sufficient numbers to allow the election of directors who would place all the management of the bank in the hands of the cashier, who used his power for his own profit.^a

One of the most common irregularities found was in the manner of protesting notes. The laws of 1835, chapter 307, section 2, forbade a bank to be in any manner, directly or indirectly, interested in the fees of any notary public who did its protesting business, and regulated the fees to be charged by an officer or clerk of a bank if also a notary. If the notary, employed to protest paper in which the bank was interested, was also a stockholder in the bank he must not receive any fees. Many banks violated this law intentionally for the profit of officers or stockholders, or in ignorance. The cashier, being also a director and stockholder, and, therefore, disqualified, would make an arrangement with a notary, by which the cashier could do the protesting, using the notary's name and paying him a fee.^b Or the officers would do the protesting business and charge higher fees than the law of 1835 permitted. In various ways the officers of banks evaded or disregarded the law. It only adds to the

^a For examples of the practices just described, with names and evidence taken by the committee, see Assem. Doc. 328, 1837, Vol. IV, pp. 27-28, pp. 31-32, pp. 39-40, pp. 43-44, pp. 45-49, especially flagrant abuses; pp. 50-55, good concrete examples of oppression. Some astonishing cases of extortion cited.

^b Assem. Doc. 328, 1837, Vol. IV, p. 41.

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volume of evidence against bank officers of this early period of banking development.

It will throw light on the sort of banking being done if some of the chief items of the bank statements of the safety-fund banks, over a period of years, are presented. The figures will be stated approximately in millions and will be given for all the banks under the safety-fund law, for the banks in New York City alone, and for all others outside of the city.

Chief items of bank statements of safety-fund banks, 1830-1842.^a

NOTE.—By city banks are meant those of New York City.

[Amounts are stated in millions of dollars.]

Year.	Total banks.	Location as to city or country.	Capital.	Circulation.	Loans and discounts.	Specie.	Individual deposits.	Profits in per cent of capital.	Circulation in per cent of capital.	Specie in per cent of notes and deposits.	Specie in per cent of capital.
1830	29	All.....	6.3	5.9	11.2	0.4	1.6	-----	94	5.3	6.3
		City.....	-----	-----	-----	-----	-----	-----	-----	-----	-----
		Country.....	-----	-----	-----	-----	-----	-----	-----	-----	-----
1831	51	All.....	18.8	12.0	32.8	1.7	5.8	-----	64	9.6	9.0
		City.....	11.3	4.4	17.7	1.2	4.0	-----	39	14.3	-----
		Country.....	7.5	7.6	15.1	.5	1.8	-----	101	5.3	-----
1832	58	All.....	20.2	12.2	35.6	1.8	7.9	-----	60	9.0	8.9
		City.....	11.9	4.2	20.8	1.3	5.1	-----	35	14.0	-----
		Country.....	8.3	8.0	14.8	.5	2.8	-----	96	4.6	-----
1833	69	All.....	22.7	15.4	43.7	2.2	8.4	-----	68	9.2	9.7
		City.....	12.6	4.9	24.4	1.6	7.0	-----	39	13.4	-----
		Country.....	10.1	10.5	19.3	.6	1.4	-----	104	5.0	-----
1834	76	All.....	26.2	14.5	52.9	5.6	14.4	-----	55	19.3	21.3
		City.....	14.6	5.0	30.5	4.4	11.6	12	34	26.5	-----
		Country.....	11.6	9.5	22.4	1.2	2.8	13	82	9.8	-----
1835	77	All.....	26.5	19.0	59.7	5.0	14.1	-----	72	15.1	18.8
		City.....	14.6	6.4	33.2	3.6	10.6	16—	44	21.1	-----
		Country.....	11.9	12.6	26.5	1.4	3.5	15+	106	8.7	-----
1836	90	All.....	32.5	22.1	67.3	5.6	15.0	-----	68	15.0	17.2
		City.....	16.6	8.2	36.5	3.9	11.2	17+	50	20.1	-----
		Country.....	15.9	13.9	30.8	1.7	3.8	16—	85	9.6	-----
1837	88	All.....	32.2	11.6	53.3	3.7	12.7	-----	36	15.1	11.4
		City.....	16.6	5.0	28.0	2.5	9.8	24+	18	19.4	-----
		Country.....	15.6	8.6	25.3	1.2	2.9	20+	55	10.4	-----

1838	89	All.....	32.4	17.7	60.3	5.9	15.2	-----	54	17.9	18.2
		City.....	16.6	4.4	30.0	4.4	10.8	17 -	26	29.0	-----
		Country.....	15.8	13.3	30.3	1.5	4.4	17 -	84	8.4	-----
1839	91	All.....	33.0	9.9	47.2	5.0	13.2	-----	30	21.6	15.1
		City.....	16.6	3.4	21.9	3.7	10.0	12 +	20	27.6	-----
		Country.....	16.4	6.5	25.3	1.3	3.2	16 +	40	13.4	-----
1840	90	All.....	32.6	14.3	49.5	4.9	15.0	-----	44	16.7	15.0
		City.....	16.6	4.1	22.8	3.8	10.6	12 +	25	25.8	-----
		Country.....	16.0	10.2	26.7	1.1	4.4	16 +	64	7.5	-----
1841	85	All.....	30.7	11.4	44.1	4.2	12.3	-----	37	17.7	13.6
		City.....	16.7	4.1	21.8	3.3	9.4	10 -	25	24.4	-----
		Country.....	14.0	7.3	22.3	.9	2.9	16 -	52	8.8	-----
1842	81	All.....	29.5	8.9	40.9	5.9	13.6	-----	30	26.2	20.0
		City.....	15.3	3.4	21.3	4.9	10.9	8 +	22	34.2	-----
		Country.....	14.2	5.5	19.6	1.0	2.7	15 -	39	12.2	-----

^a For the figures used as a basis for the calculations of the table see "Reports of the Bank Commissioners" in the assembly documents year by year. Miss Hasse's list of documents for New York banking will give the number and volume of these reports. The figures given in the January report of each year were taken for the preceding year. Thus the figures found in the report in January, 1831, were taken as covering the year 1830, etc. In the reports the New York city and country banks were not reported separately until January, 1835, but the statements for the New York City banks for 1831, 1832, and 1833 were given in the report of the bank commissioners for 1837 (Assem. Doc. 78, 1837, Vol. II, p. 18). By using these items and the totals for all safety-fund banks the amounts for the country banks during these years were found. The figures are presented in millions and tenths. The percentage of profits on capital was estimated from figures given also in the bank commissioners' reports. They are not necessarily an accurate index of dividends actually declared. In the report of the bank commissioners for January, 1835, the dividends of the banks are given for 1831, 1832, 1833, and 1834, classified in four groups, according to the size of capital and location in city or country. The rate of dividend is given for each group. The New York City banks are put in one group, and the country banks are classed in three groups, according as their capitals are \$100,000 and under, \$100,000 to \$200,000, and over \$200,000. The \$100,000 group shows the largest dividends and the city group the lowest. For the details see Assembly Document 74, 1835, Volume II, page 20. It is not to be understood that profits, as presented in the table, mean the same as the dividends actually declared. The city banks especially probably kept a surplus and did not divide up all the profits as dividends. The country banks would probably not keep so large a surplus, if any. The large profits help to explain the pressure for new banks. The last three columns of the table were calculated from the figures given in the table and are only approximate, but were carefully calculated.

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A comparison of the above table with the one setting forth the items of the city and country banks in Chapter I will show in general the same differences existing between the city and country banks. The city banks, during the period covered in the table, issued notes to an amount varying from between a third and a half of their capital, during the first half of the period, to one-fourth or one-fifth during the second half of the period. The country banks, on the other hand, issued an amount of notes which exceeded the capital during the first part of the period and decreased to even less than half in some years during the latter part of the period. Taking all the banks, the notes compared with capital tended to decrease during the period. The deposit business was growing in both city and country banks, but especially in the city. In the table in Chapter I it was observed that the city banks kept an amount of specie equal to about one-seventh of their demand obligations of notes and deposits and the country banks about one-twentieth. In the table just presented it appears that the city banks begin the period with about the same proportion as before, but during the period the specie increases until they hold one-fifth and one-fourth, and even more. The country banks, as shown in next to the last column of the table, also increased their specie from about one-twentieth of the notes and deposits to about one-tenth. Taking all the banks, it will be clear that there was during this period a distinct increase in the specie basis of banking. The table also makes clear that the agitation for the suppression of notes under \$5 during 1834 and 1835 and the passage of the law in the

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latter year did help to infuse more specie into the circulation, as its advocates claimed it would do.

The last column of the table was calculated for all banks under the safety fund in order to meet a charge, sometimes made, that as the capital invested in banking increased the amount of specie was divided up among the larger number of banks, and therefore the relative amount compared with capital decreased. This will be disproved by a glance at the percentages.

It will be observed from the table that there was a steady increase in banking capital, circulation, loans, and deposits until 1836, when a climax was reached. All these items had about doubled within a period of six years. It was a period of rising prices and speculation which was sure to be followed by the results of over-expansion. The profits of the banks, as shown in percentage of the capital, steadily increased during the period up to and including 1837, with a slight advantage in favor of the city banks. This does not seem to accord with the gloomy predictions of the New York City banks when the safety-fund law was passed. They declared then that it meant ruin for them and that they could not bear the pressure of the extra tax of one-half of 1 per cent, while, because of their large dividends, the country banks were quite able to bear the tax to create the fund. During the period of liquidation following 1837 the profits declined, and now the advantage was distinctly on the side of the country banks. The city banks were at a disadvantage during the period when trade was deranged and the exchanges in confusion as a result of the recent panic. The country banks were not so severely affected,

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because not so intimately connected with the great center of the nation's trade and industry.

It was a matter of serious concern in the minds of many as to how the safety-fund banking system would endure the pressure of panic. There had been many warnings of revulsion in trade. Our imports had been rapidly increasing over exports. Three European houses had extended credits to the United States to the extent of about \$19,000,000, which further stimulated trade. The reaction began by a check on our credit abroad and the sending home of our protested bills. There was a sudden demand for specie to export. As the above table shows, the specie in the city banks rapidly decreased during 1837. Demands by depositors, followed by a run on the city banks, completed the panic, and specie payment was suspended in New York City May 10.^a The commissioners go on to assert that the suspension was not the result of defects in the organization of the banks, but was an incident to their connection with the commercial interests of the country. It was, however, the fault of the banks that they were not better prepared to meet the emergency. They could have weathered the domestic revulsion, but the foreign reaction was unexpected. The commissioners considered the debts of the banks to be sound and predicted that their losses would not be great. The table, before presented, will show how the loans were curtailed in 1837 and the circulation reduced about one-half. The commissioners' report presents the aggregate liabilities of all the banks to the public on January 1, 1837, as \$82,444,841, which

^a Assem. Doc. 71, 1838, Vol. III, pp. 4-5. Bank commissioners' report.

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had been reduced by January 1, 1838, to \$49,434,459.^a The immediate resources of the New York City banks to meet immediate liabilities were 63 per cent of the liabilities at once due. This showed strength on the part of the city banks at the time when the commissioners reported—January, 1838. An arrangement had been effected between the city and country banks under which the notes of all the banks of the State were current at par in the city. Banks sacrificed the discount formerly paid by the public. The arrangement inspired confidence between the banks, lessened the rate of exchange, and facilitated the intercourse between city and country. It was feared that, since specie payment had been suspended, banks would issue notes to a dangerous amount. Therefore, on May 16, 1837, soon after suspension, the legislature passed a bill further restricting the issue of notes. Banks, under the law of 1829, were permitted to issue to an amount equal to twice their capital; but under this new law banks could issue as follows:

Bank-note issue authorized by law of May 16, 1837.^a

Capital.	Notes.	Capital.	Notes.
\$100,000	\$150,000	\$500,000	\$350,000
120,000	160,000	600,000	450,000
150,000	175,000	700,000	500,000
200,000	200,000	1,000,000	800,000
250,000	225,000	1,490,000	1,000,000
300,000	250,000	2,000,000	1,200,000
400,000	300,000		

^a For text of law see *Semiweekly Argus*, May 19, 1837.

These restrictions were not severe, because it was the small bank that issued the largest proportion of notes,

^a Assem. Doc. 71, 1838, Vol. III, p. 6.

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and the large city banks did not wish to avail themselves of the power of note issue even up to the limit set by the new law, if we are to judge by the past experience of the city banks. The commissioners call attention to the fact that all the banks in the State had been authorized to issue \$68,625,000 in notes; but under the new law the same banks could issue only \$29,590,000.^a

The year 1837 brought the first call upon the safety fund, which had been accumulating from the contributions of the banks since 1831. The commissioners found it necessary to proceed against three Buffalo banks for violations of the law which endangered their ultimate solvency. Injunctions were issued against them. Then it was discovered that the law of 1829 provided for the payment of the debts of failed banks only after the assets of the banks were settled up and the balance ascertained. It was perceived at once that the note holders of failed banks would lose through the depreciation of their notes awaiting payment. Consequently the legislature passed an act, in May, 1837, enabling the authorities to take measures to pay the notes of failed banks at once out of the fund, and thus prevent depreciation and loss to the note holders. It allowed the comptroller to use his discretion as to the measures to be employed. After the other creditors of the failed bank should be satisfied the amounts thus paid from the safety fund for notes were to be repaid to the comptroller from the remaining assets of the bank, if any were left. If after a final settlement of the affairs of the failed bank the fund was not

^a Assem. Doc. 71, 1838, Vol. III, p. 12.

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repaid and was thereby decreased, the solvent banks were to be called upon to make good the deficiency by renewed contributions.^a The Canadian banking law provides that the notes of failed banks shall bear interest at 5 per cent until redeemed from the safety fund. This prevents depreciation and the sale of the notes at a loss. However, the notes are redeemed at once from the fund and the fund repaid from the assets of the failed bank. The notes, moreover, are a first lien upon the assets of the failed bank.

As soon as the act, above described, was passed the chancellor of the court authorized the comptroller to take such measures as he deemed necessary to redeem the notes of these three Buffalo banks. Their outstanding circulation, as reported by the bank commissioners, aggregated \$413,961. The comptroller gave public notice that the bills of these banks would be received in payment of canal tolls and all other debts to the State. This gave credit to the bills in actual circulation. Considerable sums were thus received by the State and redeemed from the bank fund, but all advances thus made, together with interest at 7 per cent, were repaid to the fund by the several banks for whose notes they were made. The three Buffalo banks were allowed to continue under certain restrictions imposed by the court, but later they all failed hopelessly.

In the same year the legislature repealed the charters of two banks, the Sackett's Harbor and the Lockport, for violation of the banking laws. The comptroller took

^a For text of act see *Semiweekly Argus*, May 23, 1837.

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the same measures, as in the case of the Buffalo banks, to redeem the notes of these banks. Shortly afterwards the Sackett's Harbor Bank was allowed to revive its charter and all advances out of the fund, for the redemption of its notes, were repaid with interest. The affairs of the Lockport bank were settled in such a manner as to leave the safety fund practically undiminished in 1840 when the first really serious failures began.^a

The bank commissioners, in their report for January, 1839, commend the banks of the State because "they were enabled to take the lead in the resumption of specie payments."^b Resumption took place with apparently little agitation, and the losses did not seem to be as great as expected. All the banks, except the Oneida and Brooklyn banks, whose capitals had been impaired previous to the revulsion, in their annual reports showed "a surplus of profits on hand, after deducting bad debts."^c It might be questioned, in view of the future failures of some of these banks, whether the officers had the courage or the desire to count as bad all the debts that should have been so classed. The commissioners, in fact, express uncertainty as to the proportion of debts that may yet prove bad, and that, consequently, may impair the capital. The officers hesitate to withhold dividends, and so are slow to count as bad debts the doubtful cases.^d When we see the figures for the assets of the banks which later failed and the amounts realized from them by the receivers,

^a L. Carroll Root: *Sound Currency*, Vol. II, No. 5, p. 8.

^b *Assem. Doc.* 101, 1839, Vol. III, pp. 3 et seq.

^c *Ibid.*, p. 5.

^d *Ibid.*, p. 6.

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we shall be forced to conclude that many bad debts were not charged to the loss account at this time. Dividends were forbidden by the legislature during suspension in 1837. Therefore dividends were especially large the following year. As seen in the table, before presented, the profits were reported for 1837 and stood especially high, being 24 and 20 per cent of the capitals of the city and country banks respectively. For 1838, the profits reported were 17 per cent in both classes of banks.

The readjustment after the panic of 1837 was not quickly or easily made by the banks. The table, before presented, shows the items rising and falling in spasmodic attempts to regain the normal state. The report in 1838 stated that the banks in the country had generally extended their circulation to the limit allowed by the law of 1837 and complaints were made that the limit was too low. The commissioners thought "the range of circulation, under the law as it is, high enough."^a A very important fact as to circulation was also pointed out, that the amount of circulation which a bank can sustain depends upon the local situation as much as upon the amount of its capital.

The report of 1840 described another financial disturbance during which "the pecuniary distress of the last autumn was decidedly more intense, more general, and more embarrassing than any that has occurred since our acquaintance with the subject."^b By this time the free banks organized under the general law of 1838 were in operation. The whole situation was aggravated by "the

^a Assem. Doc. 101, 1839, Vol. III, p. 8.

^b Assem. Doc. 44, 1840, Vol. II, pp. 4 et seq.

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practical operation of the two systems of banking.” They were organized on different principles and their restrictions were not uniform. The general result, not anticipated, had been to contract the volume of currency. This is how it happened. It was supposed that the banks under the general law were not subject to the restrictions of the Revised Statutes as to buying their own notes at a discount in the market. The safety-fund banks were not allowed to do this. Buying their own notes, as well as those of the safety-fund banks, at a discount proved more profitable for the free banks than the discount business, and, besides, tended to displace the notes of the safety-fund banks, for which they were readily exchangeable. This would account for the large redemptions of safety-fund banks during the summer of 1839. This situation lessened the ability of the safety-fund banks to discount, since their notes issued were rapidly collected by free banks and sent home for redemption. The free banks, moreover, many of them, were not furnishing discounts to any great extent, but doing a business in “shaving” their own notes and the notes of the other banks.^a Embarrassment to borrowers was the natural result. Besides, the withdrawal of capital to invest in the stocks of other States, to be deposited with the comptroller under the general banking law to secure the issues of notes, and the suspension of specie payment in other States contributed to the distress. It is to the credit of the New York banks that under such conditions they did not suspend specie payment a second time.

^a Knox: History of Banking in United States, p. 416.

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The system of redemption of the country-bank notes had become deranged and the paper was at a great discount in the city in 1839. This was due to the discontinuance of the voluntary arrangement between city and country banks during the panic by which country notes were kept at par and the banks divided the expenses of redemption instead of making it a charge upon the public. But the city banks had found the burdens of redemption, under the conditions above described, too heavy, and had discontinued the arrangement. Confusion resulted, and discounts on country notes ranged as high as 6 per cent.^a This was a great source of profit to those who "shaved" notes and a high tax upon the public. It will be observed from the table, before given, that the circulation of the city banks had been reduced in 1839 about 25 per cent, while that of the country banks had decreased about 50 per cent. Of course the above conditions affected the country-bank circulation more severely. This confusion of 1839 became intolerable, and in May, 1840, the legislature passed a law requiring all banks, whether free or safety-fund, outside of New York, Brooklyn, or Albany, to appoint an agent and open an office in New York or Albany for the redemption of their notes at not more than one-half per cent discount. The commissioners' report in January, 1841, stated that the law was operating with great success and was producing general uniformity in the value of country paper. The promptness of the country banks to redeem produced confidence in the soundness of their condition.^b

^a Knox, p. 408; also Assem. Doc. 44 1840, Vol. II, pp. 6 et seq.

^b Assem. Doc. 64, 1841, Vol. III, p. 6.

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The bank commissioners again called attention to the fact that the vice of banking had always been to invest in "accommodation paper." The effect was to increase or decrease the currency according to the supposed wants of business rather than its real needs. Banks should confine themselves more to business paper as security for loans and discounts.^a The commissioners in 1841, in contrasting the free banking system with the safety-fund system on this point, pointed out that the free banks could not use their capital to any extent in their discounting because it was invested largely in securities deposited with the comptroller for notes issued. Their ability to make excessive issues was restricted. They could not rely upon these securities to provide for the ordinary redemption of notes, but must rely upon payments due on notes discounted. They must, therefore, confine their loans to business paper on short time and paid at maturity as a general rule. The profits of note issue were not so great under this system, because of the necessity of a dollar-for-dollar security, purchased and deposited with the comptroller. The safety-fund banks, on the other hand, had entire control over their capital and employed it, together with their credit, in discounting and issuing notes. The profits which came to the safety-fund banks from this privilege produced "an unavoidable tendency toward excessive issues." The banks were tempted to loan on accommodation paper to keep their notes out and facilitate enterprises that were either doubtful or required a long time to enable them to repay the loan.^b In this

^a Assem. Doc. 44, 1840, Vol. II, p. 16.

^b Assem. Doc. 64, 1841, Vol. III, pp. 10-12.

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temptation of the safety-fund banks we find much to explain the worthless assets of the banks whose failure we are now about to describe.

2. BANK FAILURES 1840-1842; CAUSES.

During the years 1840-1842 bank failures followed one upon another in rapid succession, in the order named below:

- (1) City Bank of Buffalo.
- (2) Wayne County Bank.
- (3) Commercial Bank of New York City.
- (4) Bank of Buffalo.
- (5) Commercial Bank of Buffalo.
- (6) Commercial Bank of Oswego.
- (7) Watervliet Bank.
- (8) Clinton County Bank.
- (9) Lafayette Bank, New York City.
- (10) Bank of Lyons.
- (11) Bank of Oswego.

Some causes of these failures we have already suggested in general terms. Three of them had secured their charters in 1834 and five more in 1836, when the mania of speculation was at its height. Thus eight, out of the total of eleven, had begun their careers under the immediate temptation to reckless banking, under the direction of officers who in some cases had shown an almost incredible disregard of any interests but their own private gains. There had been charges of political motives in granting some of these charters and there existed a bad system of stock distribution, already described in detail, by which there was the chance that the

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stock of a bank would fall into the hands of a few men who were interested primarily in the speculative side of banking. Stockholders secured the funds with which to purchase stock by borrowing it and, in some cases, hypothecating the stock of the new bank as security. Then, the next move was to secure a loan from the new bank, after it opened for business, in order to repay the old loan. Thus, was more than one bank weakened, because its stockholders did not really possess capital to invest in banking, but themselves borrowed in order to reap the profits from the ownership and sale of bank stock. The investigations of 1835 and 1837, which have been detailed in the preceding pages, revealed certain evils which legislation tried to remedy to some extent, but which showed the greed of bank officers; the lack of moral responsibility on the part of directors and officers to the stockholders and to the public; and the conception of banking, even the privilege of note issue, as a private business, organized purely for gain. There had been too much loaning to officers and directors, sometimes for questionable purposes, and often on insufficient security. There had been too large loans to individuals, and often upon paper created to secure the loan, and often renewed at maturity, that is, upon accommodation paper rather than upon business paper falling due in a short time and not often renewed. The country banks, in order to increase profits, were constantly tempted to extend their note issues beyond prudent limits, and upon doubtful security. The public, moreover, were not so watchful as to the notes, because the resources of all the banks were pledged to secure the notes of each one. It was, there-

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fore, easier, if the bank officers were willing to take the risk, to force a large circulation upon the public, not always in response to the needs of trade. There had not yet developed a proper theory of reserves for the demand obligations of a bank in notes and deposits. In fact, those interested in banking seemed so unconscious of the rapidly developing deposit business and its claim to a reserve to meet demands, that when the serious failures occurred they were surprised that the law of 1829 had made the fund responsible for anything but notes. Too little specie was kept as a basis for sound banking, but this defect, too, was in process of remedy. It is noteworthy that only two of the banks that failed were New York City banks, and one of these paid its obligations to the public in full without withdrawing anything permanently from the bank fund.

The specific causes of failure for each bank, so far as we have been able to gather them, will now be presented:

CITY BANK OF BUFFALO.

In a debate in the legislature in 1841 on this bank the charge was made that it had begun business in 1836 without real capital. The subscribers for stock gave their notes to secure the money with which to pay up the capital stock.^a It was also stated in debate that John B. Macy, the president of the bank, was indebted to the institution to the amount of about \$100,000 on doubtful security, and another officer to the amount of \$60,000 on fancy stocks and corner lots in Toledo.^b The Argus

^aSemiweekly Argus, Jan. 26, 1841.

^bSemiweekly Argus, Feb. 2, 1841.

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of February 7, 1840, issued a few days after the failure of the bank, quotes the charges of distribution of the stock of the institution to politicians at the time of its organization, and, in an editorial, points out the fact that a part of the state canal funds are in the bank, intimating an attempt on the part of state officers to support the bank.

The bank commissioners asked for an injunction and a receiver in November, 1839. The hearing was set for the first Tuesday of December and, in the meantime, a temporary order was granted. The bank asked for an extension, which was granted until January, 1840, and then until February 3, 1840. On the latter date no one appeared for the bank and the receiver was appointed. In March the receiver reported that some of the books were not posted up and that the accounts with persons and banks "were in an unsettled state."^a Much real estate was held by the bank as security. It appeared that, after the injunction had been served, some of the officers made an arrangement with certain individuals "whereby an attempt was made to extinguish certain debts, and to create liabilities against the same in violation of the injunction and in fraud of said bank."^b It seems that too long a time elapsed between the request for an injunction and the final hearing, which gave an opportunity for this attempt at fraud on the part of the officers. Certain securities were given up to debtors of the bank in exchange for property worth very little. This was done through a committee of directors which never reported.

^a Assem. Doc. 87, 1841, Vol. IV.

^b Assem. Doc. 108, 1841, Vol. IV; also Doc. 144 in same volume.

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The assets showed reckless banking or bad judgment.

Bonds and mortgages were held by the bank, valued at	-----	\$178, 508
Which the receiver estimated at	-----	67, 534
Bills discounted, considered "good"	-----	64, 360
Bills discounted, considered "doubtful"	-----	83, 643
Bills discounted, considered "bad"	-----	182, 850

"The receiver is of the opinion that from the whole amount of bills discounted, the sum of \$100,000 may be realized."^a The names of the makers of the paper discounted are given on pages 22-32, and there was probably a large quantity of "accommodation paper." There were large debts to officers and directors without good security.

WAYNE COUNTY BANK.

The bank commissioners reported to the legislature on the affairs of this bank.^b It was directed chiefly by the cashier until May, 1840, when he resigned. He was given a free hand by the directors and large profits became the ruling purpose. Improper practices resulted. The cashier, according to report, practically chose the directors through the proxies of nonresident stockholders. The commissioners regarded this lack of care on the part of the directors as the chief cause of what followed in the history of the bank. The cashier, tempted by his power, engaged in speculation for years and drew large sums from the bank by discounts to others who were ostensibly interested in the speculations, but who were used really to disguise the loans on the books, so that the cashier's name might not appear. Doubtful securities were substituted for what were probably good ones at first. When the

^a Assem. Doc. 87, 1841, Vol. IV, p. 33.

^b Assem. Doc. 172, 1841, Vol. V.

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new officers came to readjust the affairs of the bank, they found worthless securities and bad debts.

COMMERCIAL BANK OF NEW YORK CITY.

This bank was also the victim of its cashier and the speculation of the times. It was charged with the loss of more than one-half its capital and an injunction granted. The bank had purchased, in September, 1841, from its late president, \$140,000 of its own stock at 20 per cent below par, and had applied about \$55,000 of this stock to the payment of a debt due the bank from the president. Valuable securities were allowed to be withdrawn and others substituted that were doubtful. The cashier embezzled \$56,000, concealing it by a memorandum counted as cash. He put in circulation bills of the bank for his own benefit without recording them on the note register. He had continued such practices for four years, beginning during the mania for speculation in 1836-1837. Speculation was not confined to the cashier.^a Here are some of the items still due the bank in 1843:^b

Bills discounted, under protest.....	\$288,212
Loans on stocks or other securities.....	115,059
Overdrafts.....	71,959
Defalcation of late cashier.....	56,000

BANK OF BUFFALO AND COMMERCIAL BANK OF BUFFALO.

The Buffalo banks, it will be remembered, had been already under injunction in 1837. They had apparently been closely watched by the commissioners. They had been examined for a period of a week in July, 1841.

^a Assem. Doc. 29, 1842, Vol. II, pp. 12-13.

^b Assem. Doc. 75, 1843, Vol. III, p. 1.

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They possessed assets of real estate, bonds, mortgages, and personal securities, unavailable for banking purposes, at least under pressure. But it was represented by the officers that most of these assets were worth the valuation on the books of the bank. It was not possible to determine what part of the capital was impaired. The commissioners could not, therefore, apply to the court. In one of these banks there was a debt against a single firm, of which the late president, now deceased, had been a member, to the amount of one-half the capital of the bank, besides a large personal debt against the late president himself. This joint debt, incurred before 1839, had been secured during that year by a mortgage on property in another State, which has since proved of little value.

In October, 1841, it was discovered that the Bank of Buffalo had issued notes beyond the legal limit. An injunction was granted within ten days. It was found, however, that during this time many of the depositors had become alarmed and had withdrawn their funds. They were paid in bills of the bank—an utter violation of law.^a The commissioners in 1843 declared, concerning this bank, that the nature and magnitude of the frauds were “unprecedented in the history of banking in this State.”^b Other overissues were discovered when the comptroller began to redeem the notes out of the safety fund. Already, at the time of this report, January, 1843, the comptroller had redeemed \$237,731 over the legal limit, which exceeded the amount given in the engraver’s

^a Assem. Doc. 29, 1842, Vol. II, pp. 14-16 for above.

^b Assem. Doc. 34, 1843, Vol. II, pp. 16 et seq.

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account by about \$143,000.^a In November, 1842, the three commissioners consulted the books of the bank again, and summoned officers and directors. It was shown that the officers had sworn falsely in their reports. They were indicted for perjury.^b

In November, 1841, the Commercial Bank was examined and an overissue of \$180,000 was found. The cashier swore that these notes were in the possession of agents at New York and Albany and had been redeemed. It was discovered, on inquiry at Albany, that the president of the bank had received notes to a large amount from the redemption agents, but had again put them in circulation. An injunction was at once secured. The overissue amounts to about \$190,000, but about \$60,000 of this amount the bank claims as its property, not in circulation.^c There were no penalties upon bank officers for overissue, but penal enactments would not have been adequate to reach the evil. Registration of notes by a state official was needed.

COMMERCIAL BANK OF OSWEGO.

The bank commissioners in 1842 reported that it was understood that this bank, when organized in 1836, fell under the control of irresponsible persons, and that its funds were, to a large extent, applied to the payment of shares, and to the private speculations of its managers. The management changed in 1840 to men of known integrity, but in April, 1840, the bank was found in an

^a Assem. Doc. 34, 1843, Vol. II, p. 19.

^b Ibid., p. 20.

^c Assem. Doc. 29, 1842, Vol. II, pp. 14-16 for above.

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embarrassed condition. The books showed a debt against one person to an amount equal to one-half the capital. Large sums were long overdue, with poor security. The effort to save the bank was of no avail.^a

WATERVLIET BANK.

The cashier fled in 1841, at the discovery of gross frauds over several years. These had been concealed by false entries and perjury. A new cashier was appointed, but, owing to the depreciation of securities, the bank could not proceed. The failure was brought about by allowing the entire care of the affairs of the institution to rest in the hands of a single officer.^b The bank had hypothecated its own notes, which, although not illegal as long as within the authorized limit of issues, was bad banking.^c At the sale of the assets of the bank, the comptroller, through his agent, bought the following:

Notes and drafts against Peter Comstock	\$113,098
Bonds and mortgages of Peter Comstock	106,000

The comptroller thinks that very little can probably be collected on these. It shows too large loans to an individual on poor security.^d

CLINTON COUNTY BANK.

This bank suspended payment of its notes at its agency in Albany in December, 1841.^e Its credit was so affected by this suspension, temporary though it was, that its

^a Assem. Doc. 29, 1842, Vol. II, pp. 16-18.

^b Assem. Doc. 34, 1843, Vol. II, pp. 7-8.

^c Semiweekly Argus, July 19, 1842. Statement from the comptroller's office, July 13, 1842.

^d Assem. Doc. 4, 1848, Vol. I, p. 77, comptroller's report.

^e Assem. Doc. 29, 1842, Vol. II, p. 18.

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whole circulation came in for redemption, and the bank failed in April, 1842. It, too, was chartered in 1836, and for several years had been "almost exclusively managed by its president and cashier without the care or supervision of the board of directors." The officers appropriated the funds to private purposes or for their favorites in the shape of loans and discounts. These speculations by the officers threw heavy losses upon the bank, because the security given for the loans proved worthless.^a

LAFAYETTE BANK OF NEW YORK CITY.

An injunction was granted on the ground that this bank had lost over one-half of its capital. It has met all its claims to the public and one-half of its capital stock. Large loans to its directors and others for speculation caused the failure.^b

BANK OF LYONS.

Chartered in 1836, this bank is said to have fallen under the control of two persons who paid large premiums to secure a majority of the stock. These persons borrowed money to do this, and then repaid it by abstracting the amount from the bank, and depositing notes and securities. About three years before failure, a new management came into power and tried to save the bank, but a serious decline in the assets, which were not readily convertible, made the task an impossible one.^c

After the affairs of these banks, which had failed during 1840-1842, had been settled in part by the receivers, the senate, impatient at the delay and suspicious that

^a Assem. Doc. 34, 1843, Vol. II, pp. 14-15.

^b *Ibid.*, p. 6.

^c *Ibid.*, pp. 15-16.

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the receivers might not be very faithful in all cases, asked their committee on banks in 1845 to investigate the affairs of the receivers and report.^a The following from that report throws much light upon the causes of failure:

Bank.	Amount of assets at time the receiver took charge.	Amount realized from assets sold.	Amount of assets unsold in 1845.	Estimated value of unsold assets.
City Bank of Buffalo.....	\$739,017	\$166,576	\$570,000	\$50,405
Bank of Buffalo.....	1,221,843	82,837	-----	-----
Commercial Bank of Buffalo ..	985,064	172,864	456,447	49,690
Wayne County Bank.....	293,970	56,744	246,201	22,628
Bank of Lyons.....	385,608	37,445	236,229	11,524
Bank of Oswego.....	213,353	32,693	163,813	-----
Clinton County Bank.....	543,430	76,019	64,382	12,753
Commercial Bank of New York.....	858,472	303,339	301,406	-----
Watervliet Bank.....	202,379	19,459	204,137	-----
Commercial Bank of Oswego..	507,173	80,653	94,087	10,525

These assets tell a story of reckless and fraudulent banking, culpable conduct on the part of officers, and the ordinary depreciation that always accompanies a period of panic.

Now, the chief items in the bank statements of at least a part of the insolvent banks, over the period from their organization until their failure, may prove enlightening as to the kind of banking done during solvency. It must be admitted, however, that the developments following failure showed that, in some cases, false statements had been made. Bank officers were not apt to show in their reports a dangerous state of affairs, and we have the bank commissioners' statement that the banks prepared for these annual reports by curtailing loans, etc.^b

^a S. Doc. 118, 1845, Vol. III, p. 6.

^b Assem. Doc. 29, 1842, Vol. II, p. 20.

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Chief items of annual statements of banks that failed, 1840-42.

[Amounts are expressed in thousands of dollars.]

Name of bank and capital in full. ^a	Year.	Loans and discounts.	Circulation.	Specie.	Deposits.	Dividends in per cent of capital.
1. City Bank of Buffalo (capital, \$400,000) ----	1836	298	105	32	41	(b)
	1837	661	235	19	50	(b)
	1838	656	298	41	58	(b)
	1839	703	269	13	13	(b)
2. Wayne County Bank (capital, \$100,000) ----	1830	-----	195	7	-----	-----
	1831	-----	169	5	-----	-----
	1832	244	157	6	-----	13
	1833	249	159	7	-----	-----
	1834	237	137	8	11	10
	1835	238	150	14	18	10
	1836	218	130	10	9	10
	1837	224	114	10	11	-----
	1838	246	141	10	23	15
	1839	228	119	9	29	10
	1840	250	144	4	6	-----
3. Commercial Bank of New York (capital, \$500,000) -----	1834	713	109	42	105	-----
	1835	1,151	189	50	224	7 1/2
	1836	1,092	217	51	166	8
	1837	809	183	52	85	4
	1838	754	230	57	84	8
	1839	769	157	51	123	8
	1840	776	121	55	129	8
	-----	-----	-----	-----	-----	-----
4. Bank of Buffalo (capital, \$200,000) -----	1831	-----	129	13	-----	-----
	1832	285	122	19	-----	8
	1833	299	164	34	-----	-----
	1834	384	134	33	45	8
	1835	427	226	30	66	8
	1836	459	182	36	87	8
	1837	417	181	22	54	4
	1838	439	187	26	92	8
	1839	360	123	25	125	8
	1840	386	196	16	123	-----
	-----	-----	-----	-----	-----	-----
5. Commercial Bank of Buffalo (capital, \$400,000) -----	1834	568	192	84	85	-----
	1835	653	273	47	114	8

^aFor the basis of the figures in these tables, see the report of the Bank Commissioners for the various years, in Assembly Documents.

^bNo dividends.

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Chief items of annual statements of banks that failed, 1840-42—Continued.

Name of bank and capital in full.	Year.	Loans and discounts.	Circulation.	Specie.	Deposits.	Dividends in per cent of capital.
5. Commercial Bank of Buffalo, etc. (continued).	1836	701	152	43	153	-----
	1837	622	237	21	51	-----
	1838	635	298	30	96	19
	1839	640	155	32	134	4
	1840	642	247	40	223	8
6. Commercial Bank of Oswego (capital, \$250,000)-----	1836	415	160	20	25	-----
	1837	361	144	11	14	4
	1838	416	182	21	26	5
	1839	497	142	9	21	8
	1840	402	216	8	52	-----
7. Watervliet Bank (capital, \$250,000)-----	1836	476	83	17	54	-----
	1837	383	42	17	36	4
	1838	450	161	17	53	12
	1839	392	97	6	52	4
	1840	410	119	12	28	9
	1841	400	115	3	23	-----
8. Clinton County Bank (capital, \$200,000)---	1836	262	95	20	16	-----
	1837	248	54	11	15	-----
	1838	336	125	11	21	14
	1839	336	125	11	21	-----
	1840	397	194	11	20	8
	1841	347	168	5	7	-----
9. Lafayette Bank, New York City (capital, \$500,000)-----	1834	690	98	47	79	-----
	1835	841	141	58	127	7 1/2
	1836	1,059	205	106	135	8
	1837	717	34	41	110	4
	1838	760	101	33	124	12
	1839	660	91	27	84	4
	1840	583	95	33	167	-----
	1841	477	72	51	63	3 1/2
10. Bank of Lyons (capital, \$200,000)-----	1836	337	182	24	14	-----
	1837	355	172	9	14	-----
	1838	343	166	17	19	12
	1839	323	125	8	12	8
	1840	310	115	10	23	-----
	1841	290	81	10	11	-----

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The statements, just presented, add little to what has been already described in the banking practices of the period. Too little specie was kept on hand to enable the banks to withstand pressure. In some of these banks the circulation was not contracted with prudence as the panic came on. We must consider the figures given in connection with the practices described as causes of failure. The loans and discounts may not appear excessive, but if a large amount is loaned on accommodation paper, often renewed, or to the officers or others on poor security, then in time of pressure the condition of the bank becomes serious. The circulation may not even approach the legal limit, and yet, if many of the notes are put in circulation on paper which had no immediate connection with past business transactions, and which is not likely to be paid at maturity, the resources of the bank endanger its solvency. In several of the banks it is evident that the specie fluctuated rapidly with the demands for note redemption, or the demands of depositors. The average dividends were not excessive, but they varied much from year to year.

The commissioners, in their report in January, 1842, declared that "confiding to the president or cashier, as the case might be, the unrestricted control over the affairs of the bank has, in our judgment, largely contributed to the downfall of all the safety-fund institutions which have failed during the past year."^a When the directors were thus neglectful, the temptation of the officers was often too strong and they and their friends

^a Assem. Doc. 29, 1842, Vol. II, p. 5 et seq.

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exploited the bank. The law was sometimes evaded by artifice.

It was also pointed out that the commissioners were often powerless to prevent a failure because the bank was not violating any positive law which would justify an appeal to the court for an injunction. It was often difficult to ascertain when the capital was impaired, because the officers, in order not to be compelled to suspend dividends, represented a debt as good when it was doubtful or worthless. Thus the bank might be utterly ruined before proof was secured.^a In their next report the commissioners recommended that their powers be extended so that "they may be authorized to arrest the proceedings of any bank whose operations, however conducted, shall, in their opinion, be adverse to the interests of the stockholders or the safety of the public."^b

The report in 1842 emphasized a practice of which some of the insolvent banks had been guilty, the hypothecation of their own notes as security for loans. By this practice banks that "have become embarrassed by improvidence and bad management and which, if standing on their own credit alone, would be unable to extend their already ruinous liabilities, are now enabled, upon the security of the fund, not only to sustain an unsound circulation but virtually to compel those banks which are managed with prudence and success to become their sureties."^c It does not alter the case that the pledge of notes must not exceed the legal limit. The comp-

^a Assem. Doc. 29, 1842, Vol. II, p. 10.

^b Assem. Doc. 34, 1843, Vol. II, p. 11.

^c Assem. Doc. 29, 1842, Vol. II, pp. 18-19.

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troller in his report of the following year called attention to the same evil practice and asserted that most of the banks which had failed had kept up for years by loans from banks and brokers, and, in some cases, from the canal fund, "on pledges of the notes of such banks, which were in effect a mortgage upon the safety fund."^a It is probable that high rates of interest were frequently offered for such loans. This practice of hypothecation was prohibited under severe penalties by a law passed April 12, 1842.^b It was a fact that when the comptroller began to redeem the notes of the insolvent banks from the fund, large sums were presented by banks and brokers. It is probable that at least a part of them were obtained in the manner above stated.^c

It will be evident that a part of the responsibility for these bank failures must be placed upon the imperfect system under which they occurred. The system of distributing bank stock as well as the manner in which the charter itself was secured, the lack of a system of registering the notes issued to prevent illegal issue, the use of the funds of the bank by its officers, the tolerance of the practice of hypothecation of a bank's own notes as security, were all finally remedied by amendments to the banking law, in some cases too late to prevent insolvency. Some had advocated a definite specie-reserve requirement, but it met with little favor.^d The panic of 1857 was needed to emphasize the lessons already begun as to sound banking.

^a Assem. Doc. 10, 1843, Vol. I, p. 53.

^b *Semiweekly Argus*, April 29, 1842, for full text.

^c Assem. Doc. 4, 1844, Vol. I, p. 53.

^d *Daily Argus*, Jan. 3, 1838, governor's message.

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If we are to credit the estimate of the bank commissioners and others in touch with the situation, many of the evils we have described would have occurred in any system. They put especial emphasis on the custom, so frequent, of allowing the affairs of the bank to be managed by one or two officers. They blamed the stockholders for not requiring more care from the directors, and the directors for allowing themselves to be "men of straw." But, at the same time, it was declared unfair to prevent voting by proxy. Then it was not a matter for legislation to reach, but rather for experience to show the necessity of a more rigid accountability of directors and for business progress and wisdom to put a premium on a stricter responsibility of bank officers to the public and those whom they served. Of course legislation could and did place restrictions about the election of directors and impose penalties for violation of trusts. With irresponsible persons once in control of a bank, the results which we have described in the insolvent banks naturally followed. Loans were concealed and false statements made; good securities were replaced by worthless ones, and speculation for personal gain threw large losses upon the bank because the security given for loans was not required to be first class.

Legislation had provided bank commissioners to inspect the affairs of the banks at least quarterly, and yet the governor in 1843 stated that it was evident the appointment of these officers "has not answered all the valuable ends which were anticipated."^a He could not see how such complete insolvency as had just been shown

^a Semiweekly Argus, Jan. 3, 1843, governor's message.

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to exist in some of the failed banks could escape their notice. In 1829, when this subject had been debated, some declared that commissioners would have to depend on the statements of bank officers anyway and, therefore, would not accomplish the purpose desired. Before 1837, one commissioner was appointed by the governor and senate and two by the banks themselves. After that date all were appointed by the governor and senate. Charges of political influence in appointment and of incompetency were made. If these charges were true, it may account for some of the practices of banks being overlooked. But no doubt many times the commissioners were deceived, and, by their own statement, they were often powerless to prevent practices until it was too late. Instead of increasing the power of the commissioners, however, the office was abolished in 1843. The committee which reported on this bill to the assembly declared that "experience has demonstrated that when bank officers are honest, commissioners are unnecessary; when they are dishonest, commissioners are unavailing."^a It is certain that the commissioners had accomplished more than the above statement gives them credit for, and we have preserved inspection as a part of our present banking system.^b

^a Assem. Doc. 154, 1843, Vol. VI.

^b The report of the Comptroller of the Currency of the United States, 1908, Table 66, classifies the causes of failure of 496 national banks from 1865 to 1908. He finds that the largest number of failures occurred from (a) injudicious banking and depreciation of securities, 66 failures; (b) general stringency of money market, shrinkage in values, and imprudent methods of banking, 50 failures; (c) wrecked by cashier, 33; (d) excessive loans to others, injudicious banking, and depreciation of securities, 33; (e) excessive loans to officers and directors and depreciation of securities, 29.

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3. THE ACTUAL BURDEN OF THE BANK FAILURES UPON THE SOLVENT BANKS AND THE PUBLIC.

The problem to be solved by the comptroller was how the bank fund was to be used to meet the rapidly accumulating charges upon it from insolvent banks. The act of 1837 (chapter 350), before described, gave the comptroller authority to redeem the notes of insolvent banks at once, instead of waiting until all the affairs of the banks had been settled, on condition that one-third of the fund be preserved for other debts than notes.^a But this act did not authorize the comptroller to call upon the solvent banks to replenish the fund, except under the law of 1829, which would require him to wait until all the affairs of the insolvent banks had been settled and thus find out whether the fund was permanently diminished. The act of May 26, 1841 (chapter 292, sec. 5), provided that, when the comptroller applied any money of the fund to the payment of debts of banks, and the fund was thus reduced below the sum provided for in the act of 1829 (3 per cent of capital), he might call on the safety-fund banks for an additional contribution, not to exceed one-half of 1 per cent on the capital.^b Some of the banks last chartered had not yet made up their original 3 per cent on their capital. The new law was construed by the comptroller so as to require these banks to pay double (1 per cent) until the original 3 per cent was completed. Nine banks did actually pay more than one-half of 1 per cent annually until their original 3 per cent was completed.^c This did pro-

^a Assem. Doc. 15, 1842, Vol. I, pp. 32-33, comptroller's rept.

^b Ibid., p. 34.

^c S. Doc. 145, 1847, Vol. IV, p. 49.

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duce a slight inequality between banks, due to the time of securing their charters, if we consider what a bank had to pay in any single year.

By January, 1841, the capital of the bank fund amounted to \$914,342.24. The comptroller, therefore, by the law of 1837 requiring him to keep one-third of this amount for other debts than notes, could only expend about \$610,000 in redeeming the notes of insolvent banks.^a The City Bank of Buffalo and the Wayne County Bank had failed in 1840 and their notes were being redeemed by the comptroller. Up to September, 1841, when the Commercial Bank of New York failed, the comptroller had paid out about \$428,000 to redeem notes of these two banks.^b Up to January, 1842, he redeemed \$118,631 of the notes of the Commercial Bank.^c This left the comptroller but a small part of the original \$610,000 which he felt authorized to devote to notes of insolvent banks. Then the Bank of Buffalo failed in November, 1841, with an apparent circulation of about \$290,000.^d The comptroller did not regard himself as authorized to redeem the notes of this bank without further legislation, since to do so would encroach upon the part of the fund reserved for other debts.

The bank commissioners so construed the act of 1837 as to permit the comptroller to go on redeeming notes, and the situation was also somewhat relieved by the additional contributions of one-half per cent called for

^a Assem. Doc. 15, 1842, Vol. I, p. 40.

^b Assem. Doc. 13, 1841, Vol. I, p. 51, and Doc. 15, 1842, Vol. I, p. 85.

^c Assem. Doc. 15, 1842, Vol. I, p. 39.

^d The actual circulation later discovered to be over \$400,000, due to fraudulent overissue.

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by the comptroller under the act of 1841 and due January, 1842. Other failures followed and the fund proved inadequate, since a part must be reserved for other debts than notes. The comptroller stated in his report that he could not redeem any more notes without legislation, and that the note holders must await the slow accumulation of the one-half per cent yearly contributions.^a

April 12, 1842, the legislature passed an act authorizing the comptroller, on order of the court, to take measures to redeem the notes of the insolvent banks at once, and to apply any or all of the fund to this purpose in the order in which injunctions had been granted against the banks. The fund was to be reimbursed out of the assets of the failed banks. This act also provided that, after all liabilities already incurred had been discharged, the fund should be applied to the payment of the notes only, of failed banks. It provided for a severe penalty upon bank officers who issued notes beyond the legal limit. The act further granted to the solvent banks the right to commute their annual contributions for the next four, five, or six years in the notes of the insolvent banks, allowing them interest at 7 per cent on the amounts commuted until the same would have been regularly due.^b

Sixty-four banks took advantage of the privilege of commuting in the notes of failed banks. They paid in \$477,609, which amounted to a redemption of this sum from the bank fund.^c In this advance payment of the notes of failed banks the solvent institutions were allowed

^a Assem. Doc. 15, 1842, Vol. I, p. 41.

^b *Semiweekly Argus*, Apr. 29, 1842, for full text.

^c Assem. Doc. 10, 1843, Vol. I, p. 50, for details.

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to pay in the bills of any of the insolvent banks regardless of the order in which the injunction had been granted. This was inconsistent with the law of April 12, 1842. At this time "a large portion of the outstanding notes of the insolvent banks was held by banks and brokers, where, in many cases, they had been left on deposit as security for loans."^a These holders of packages of notes pledged as security for loans ought not to have been treated the same as the general holder of notes in actual circulation. Obviously, this privilege of commuting, allowed to banks, was unfair to the general body of note holders, especially holders of notes of banks which failed early.

In May, 1843, an injunction was served on the comptroller, forbidding him to pay any portion of the bank fund to the creditors of any bank failing since the Bank of Buffalo, without reserving sufficient to pay all creditors of the Bank of Buffalo and those banks failing prior to the Bank of Buffalo. The object was to protect the depositors and other creditors of these banks.^b Until all the debts of these four banks were paid, not even the notes of the banks that failed later could be redeemed. The comptroller suggested that the legislature authorize the issue of state stock to pay all the charges on the bank fund, the stock to be redeemed out of the future contributions to the safety fund by the solvent banks.^c

During 1844 the comptroller continued to redeem the notes of the four banks allowed under the injunction

^a Assem. Doc. 4, 1844, Vol. I, p. 53.

^b *Ibid.*, p. 51.

^c *Ibid.*, p. 54.

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above mentioned. Up to September 30, 1844, he had redeemed \$1,502,170 of the notes of the failed banks, including the amount commuted.^a The amount of the bank fund at this same date was \$145,493.72. (See Assem. Doc. 25, 1845, Vol. I, p. 50.)

Inquiries were made of the receivers of the insolvent banks in December, 1844, as to the probable draft on the safety fund necessary to pay other debts than notes, after the assets of the failed banks had been applied. The receivers estimated it at \$1,017,000.^b The suggestion of the comptroller as to the issue of state stock to secure funds with which to pay all these debts was followed by the legislature in 1845, when an act was passed authorizing the issue of 6 per cent state stock, secured by the future contributions to the fund.^c

The comptroller was now in a position to settle all claims against the safety fund, whether consisting of notes or of other debts. A summary of debts paid out of the fund and the final burden on the fund, after the assets of the failed banks had been disposed of as far as possible, will now be presented.

^a Assem. Doc. 25, 1845, Vol. I, p. 32, for details.

^b Ibid., p. 51.

^c Assem. Doc. 25, 1846, Vol. I, p. 55.

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Statistics of the transactions of the failed banks with the safety fund. a

Name of bank.	Payments to redeem notes.	Other debts paid.	Receipts from as- sets, paid into fund.	Final bur- den upon fund.
City Bank of Buffalo.....	\$317,107	-----	\$99,996	\$217,111
Wayne County Bank.....	113,131	\$16,078	-----	129,209
Commercial Bank of New York City.....	139,837	146,129	7,188	278,778
Bank of Buffalo.....	435,540	149,241	-----	584,781
Commercial Bank of Buffalo.....	186,861	424,515	5,000	606,376
Commercial Bank of Oswego.....	163,162	78,352	2,392	239,122
Watervliet Bank.....	134,107	77,484	13,258	198,333
Clinton County Bank.....	71,896	156,257	-----	228,153
Bank of Lyons.....	52,898	40,053	3,761	88,990
Lafayette Bank, New York City ..	38	-----	-----	38
Not specified.....	725	-----	6,482	-----
Total.....	1,615,302	1,088,109	138,077	2,565,334

^a The figures for the City Bank of Buffalo may be verified by reference to Assem. Doc. 25, 1846, Vol. I, p. 33, for the amount of notes redeemed from the fund. Then for the final charge upon the fund, after all that could be realized from assets had been paid to the safety fund, see Assem. Doc. 9, 1851, Vol. I, in the table showing charges against the fund at that time. The rest of the first column will also be verified from the latter document, except for the Watervliet Bank and the notes "not specified." To verify the notes redeemed for the Watervliet Bank refer to Assem. Doc. 5, 1847, Vol. I, p. 40. For the amount of notes "not specified" reference must be made to the comptroller's reports following 1850, and the sums were found to aggregate \$725.

The second column will be verified from Assem. Doc. 9, 1851, Vol. I, in the table showing charges against the fund for other debts than notes, except for the Watervliet Bank. But in this same document, p. 32, the comptroller explains that since the close of the year (Sept. 30, 1850) he has issued stock to the amount of \$5,424.78 to pay the remaining creditors of the Watervliet Bank. He had already issued stock for \$72,059.31 for the debts of this bank (p. 35). The two amounts total \$77,484, which is the amount in the table.

The third column, consisting of the receipts paid into the fund from the assets of the insolvent banks, is the same as found in the table of L. Carroll Root, "Sound Currency," Vol. II, No. 5, p. 11 and in the "Report of the Monetary Commission of the Indianapolis Convention," Indianapolis, 1900, p. 240, in footnote. I have verified all these figures from the annual reports of the comptroller and the bank department, except the "not specified." Here the figures are difficult to vouch for. The particular documents from which the figures may be verified will gladly be given in detail, if desired. The last column is simply an addition of the first two diminished by the third, which gives the final charge upon the bank fund which must be made up by the contributions of the solvent banks.

Of the whole 11 banks which failed so near together only 2, the Lafayette Bank of New York and the Bank of Oswego, were able to settle with their creditors and pay

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their notes without calling upon the fund for assistance. The creditors were all satisfied after the long delay, either by payments from the fund or by the issue of bank-fund stock. The safety fund, therefore, was a claimant for the amounts subsequently realized from the remaining assets of the insolvent banks, up to the full amount advanced. As a matter of fact, only a very small proportion of the amount advanced was ever realized and paid back to the fund, as shown in the above table. The conversion of assets was slow. In some cases the receivers sold them at public auction. The comptroller, in his report for 1846, stated that he had sent an agent to such a sale of assets of the City Bank of Buffalo, to bid on any assets which seemed to be going at too great a sacrifice. He bought assets of the City Bank, to a nominal amount of \$470,000, for \$16,900.^a This shows how worthless they must have been. In cases where the receiver collected the assets, the proceeds, after the expenses were deducted, were paid to the comptroller from time to time. The third column in the table gives the summary of all such collections, and to secure the sums there given the yearly reports of the comptroller and bank department had to be consulted in order to find out what was turned into the fund from each bank's assets.

The capital of the 11 insolvent banks amounted to \$3,150,000, most of which proved a loss to the stockholders. Only one of the failed banks had a capital so small as \$100,000, one had \$150,000, three had \$200,000, two had \$250,000, two had \$400,000, and two had

^aAssem. Doc. 25, 1846, Vol. I, p. 57.

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\$500,000. Their total contributions to the bank fund amounted to \$86,279, whereas they drew upon the fund for over \$2,500,000.^a Members of the legislature, the bank commissioners, and others had frequently expressed the fear of too small banking capital, because they feared an excessive note issue as compared with resources. The small country bank usually exceeded the amount of its capital in notes, and thus the public had a larger claim upon its resources than upon the resources of a larger bank which did not issue such a large proportion of notes. The failures of 1840-1842 do not show that small banking capital proved fatal to the solvency of the institutions.

The bank fund had proved inadequate to meet the demands from all the debts of the insolvent banks even by the payment of the extra one-half per cent annual contributions provided by the law of 1841 to meet the emergency and replenish the fund. The law of 1845 had authorized assistance by the issue of 6 per cent state stock, to be redeemed by the future one-half per cent contributions of the solvent banks. The comptroller stated, in his report for 1849, that \$900,828.47 in this stock had been issued.^b This did not include the \$77,484 afterwards issued to pay the debts of the Watervliet Bank, so that altogether a little less than \$1,000,000 in state stock at 6 per cent was issued to pay the debts of the insolvent banks. The 6 per cent annual interest upon this stock was a charge against the fund and was contributed by the solvent banks. The stock was re-

^a Assem. Doc. 5, 1847, Vol. I, pp. 57-58.

^b Assem. Doc. 5, 1849, Vol. I, pp. 30-31.

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deemed as fast as convenient from the contributions to the fund.

How did the solvent banks meet the burden thus imposed? Banks chartered in 1829 took six years to pay up their 3 per cent on capital at the rate of one-half per cent annually. There were no additional contributions called for until January, 1842. Therefore, the banks chartered in 1829 and immediately following had a few years during 1836-1841—how many years depending on the year of their charter—during which they did not contribute to the fund, having paid their full 3 per cent; but banks chartered later, for instance in 1834, had just finished their 3 per cent on capital required by the original law of 1829 when the new call came to replenish the fund with an additional one-half per cent annually. After the first contributions, in January, 1842, the solvent banks were compelled to contribute the same amount, one-half per cent on capital yearly during the remainder of their chartered existence, and some charters did not expire until 1866. This was due to the fact that the safety fund had become mortgaged, as above explained, and needed the contributions in order to redeem the state stock with interest at 6 per cent.

Therefore, before 1842 the banks averaged less than one-half per cent on their capital in contributions to the fund.^a The exact percentages, as calculated from fig-

^a S. Doc. 145, 1847, Vol. IV, pp. 1-49, gives in detail the amount contributed by each bank yearly up to 1847. This document also shows how many banks commuted in the notes of failed banks, as allowed by legislature, and the amounts so paid into the fund in advance, as was explained on a previous page. It shows also how many and what banks paid more than one-half per cent and during what years, owing to the time of receiving their charter and the call for additional contributions.

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ures taken from the reports of the bank commissioners, which state the annual total contributions and total capital of safety-fund banks, ranged from one-half per cent to .13 per cent on capital before 1842, the lowest of course being in 1841, when a large part of the banks had already completed their 3 per cent contributions. The contributions following 1842 were regular, and were intended to be one-half per cent on the capital. For the whole period, 1830-1866, the amount paid by the solvent banks would average a little less than one-half per cent on their capital. The total contributed by the solvent banks during the entire period was \$3,119,999.24.^a The total payments from the fund for all the debts amounted to less than \$2,600,000, as the table already given shows. The rest was paid, mainly, for interest on the 6 per cent state stock advanced, under the law of 1845, to meet the charges against the fund at that period.

Losses to note holders before the redemption of the notes of insolvent banks; Canada's system.—As we have described, the law of 1829 did not provide for immediate payment of notes of insolvent banks from the fund, but only after the final settlement of the affairs of the bank and after the deficiency not covered by the assets of the bank had

^a This computation was made from figures taken from the reports of the bank commissioners, the treasurer's reports, and the reports of the banking department, in Assembly documents, as given in Miss Hasse's document list on New York banking. The affairs of the safety-fund banks were in the hands of the bank commissioners until 1843, when the office was abolished. Then reports were made to the comptroller, and, finally, in 1851, the banking department was established. The sum given is somewhat different from that given by Mr. Root in "Sound Currency," Vol. II, No. 5, p. 12. He gives \$3,104,999.51, which is not so different from the above as to be a serious discrepancy.

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been ascertained. When injunctions were procured against the Buffalo banks in 1837 it was perceived that, unless something could be done, the notes of these banks would depreciate while the note holders waited for their redemption or sold them at a discount. Therefore, the law of 1837 provided for immediate redemption to prevent losses from falling upon holders of notes of failed banks.

When the failures of 1840-1842 came so rapidly as to exhaust the bank fund, the same problem arose. The governor in his annual message, in 1843, recalls the fact that the safety fund was designed mainly to protect note holders and calls attention to the inadequacy of the fund in the present situation. He further states that if no part of the bills of failed banks are paid out of the assets, the safety fund can not discharge, with present means and future contributions, the obligations laid upon it for bills alone, until January, 1849.^a This shows clearly the situation of the note holders, for notes pass current as money and depend for their value upon being convertible on demand or at least exchangeable. This situation was relieved by the issue of state 6 per cent stock in 1845 to secure funds with which to redeem all the notes of all the failed banks, but the period from 1840 to 1845, when the fund could not meet all demands for redemption, caused great losses to the note holders, due to depreciation. These losses can only be estimated. The comptroller in his report, in 1845, stated that the losses to note holders by depreciation had been at least \$350,000. Not much could have been lost after his report, for provision was at once made by the act of 1845 for the redemption of the

^a Semiweekly Argus, Jan. 3, 1843

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notes.^a As shown by the bank commissioners' reports, the total circulation of the 11 failed banks at their last report before failure was \$1,723,366. Two of the banks paid their notes without assistance, which diminished the sum from which depreciation would likely result. The amount last reported, given above, was no doubt different from the amount at the time of failure and the amount reported did not include the illegal overissues, but this last reported amount of notes gives an approximation to the actual amount outstanding at the time of failure. The notes of the banks that failed first were promptly paid, to the extent of over \$500,000, and the solvent banks commuted their future contributions to the safety fund to the extent of almost another \$500,000 in the notes of insolvent banks. On these notes the depreciation could not have been so great as upon the notes left unredeemed, when the safety fund had been exhausted, until the time, in 1845, when the state stock was issued to pay the remainder. The comptroller in his report, in 1846, says, "The loss to first holders of the safety-fund notes was from 20 to 25 per cent and there has been a loss of about four years' interest to subsequent purchasers."^b This corresponds pretty accurately with the statement in the previous report of the comptroller.

The need in case of the failure of a bank is for prompt redemption to prevent depreciation. Canada, in her system, has a guaranty fund from which the notes of failed banks are promptly redeemed, but, in addition, the notes of failed banks draw interest at 5 per cent from the

^a Assem. Doc. 25, 1845, Vol. I, p. 52.

^b Assem. Doc. 25, 1846, Vol. I, p. 71.

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time of failure until redemption. This makes the notes pass current and prevents depreciation. The notes are a first lien on the assets of the bank.^a

Of course there must have been great inconvenience to the depositors of banks that failed. It is also probable that some sold their claims at a discount rather than wait until they should be settled out of the bank fund. The bank commissioners' reports show a total amount of deposits by individuals in the failed banks, at the time of the last report before failure, of \$681,204. Depositors' accounts were finally settled out of the bank fund along with other debts. The amount given in the above reports does not necessarily correspond with the actual deposits at the time of the failure of the banks. It is noteworthy how much more important a place notes held at that time than deposits. The reverse is the case to-day. Now the temptation is to expand deposit credits, then the effort, at least among the smaller country banks, was to keep a large amount of notes in circulation.

The law of 1838, which provided for the organization of banks under a general law instead of by special charter, sought to secure only notes. It required a deposit of securities to cover the full amount of the notes in the hands of the comptroller. These securities might be sold to redeem the notes of an insolvent bank. The problem was as to what securities should be accepted. At first stocks of the United States, New York State, or of any other State approved by the comptroller were accepted, as well as bonds and mortgages on real estate. This created a market for the stocks of other States, and when a bank

^a Horace White: *Money and Banking*, 3d ed., 1908, p. 382.

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failed and an attempt was made to dispose of these stocks they often depreciated in value. It took several years to convince the legislature that, while mortgage security might be very good for some purposes, it was not suitable for banking purposes, because under pressure it was not always convertible without serious sacrifice. The difference between security and availability was not at first clearly recognized.

We are, therefore, not surprised when the comptroller, in 1845, reports that the loss to bill holders in the case of insolvent free banks has been nearly 39 per cent, as compared with 20 to 25 per cent under the safety-fund system.^a As the general banking law was perfected losses became less and less. The following is a summary of the results of the sales of securities prior to January, 1849, to redeem the notes of insolvent banks, under the general law of 1838:^b

Indiana stock sold for 49.08 per cent of nominal value.....	\$449, 000
Illinois stock sold for 49.13 per cent of nominal value.....	239, 000
Arkansas stock sold for 58.77 per cent of nominal value.....	176, 000
Michigan stock sold for 72.95 per cent of nominal value.....	66, 000
Alabama stock sold for 71 per cent of nominal value.....	79, 000
New York stock sold for 92.86 per cent of nominal value.....	257, 555
Bonds and mortgages sold for 67.71 per cent of nominal value..	472, 988

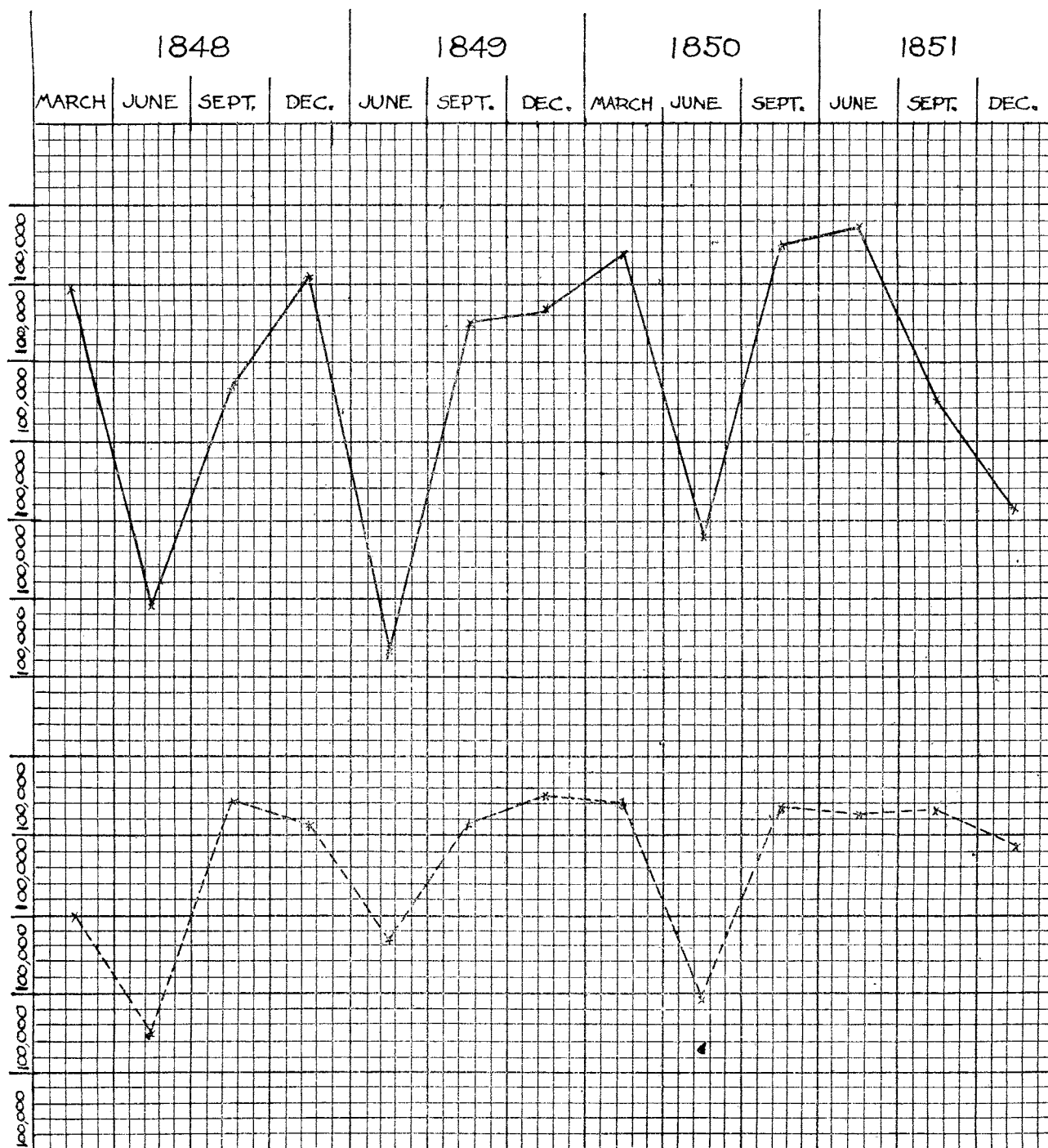
Average for all, 63.51 per cent of nominal value..... 1, 739, 543

The average for all the securities, 63.51 per cent, corresponds closely to the statement of the comptroller in 1845, given on a previous page, because the 39 per cent loss to bill holders, there stated, represents a depreciation in the value of securities deposited with the comptroller for the redemption of notes. The table shows the danger of allow-

^a Assem. Doc. 25, 1846, Vol. I, p. 71.

^b Root: Sound Currency, Vol. II, No. 5, p. 20, also comptroller's reports.

ELASTICITY OF FREE AND SAFETY FUND BANKS.



KEY:-

— Circulation of 25 Safety Fund Banks, with \$9,303,860 capital
 - - - " of 25 Free " with about the same capital

NOTE

Spaces marked represent \$100,000 each
 Small squares " " \$20,000 each

Figures for each Bank taken from the
 quarterly reports of the Comptroller

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ing the deposit of state stocks, other than New York State, as security for notes. It also makes clear that bonds and mortgages are not good security when the bank fails and the attempt is made to realize upon them at once. The defects in the law of 1838 were remedied by amendment after experience had proved the wisdom of a change. State stocks, other than New York, and bonds and mortgages were abandoned as security.

Elasticity of the two systems—the bond-deposit and the safety fund; provisions for redemption.—The basis on which the free and safety-fund banks issued notes was quite different. The free banks, especially the smaller ones, must invest a large part of their capital in certain specified securities, which were deposited with the comptroller, in return for which notes were issued to the bank, countersigned and registered. The bank officials were then permitted to sign these notes and issue them as money. The whole circulation of free banks was thus secured by a dollar-for-dollar deposit of securities, outside of the control of the bank. In case of the failure of the bank to redeem its notes promptly the comptroller was authorized to sell the securities and redeem the notes with the proceeds. The State was not responsible for the payment of the notes except to apply the securities properly to that purpose. The interest on the securities was paid to the banks which deposited them as long as these banks redeemed their notes promptly. It is clear that in many free banks a large proportion of the capital was beyond their control.

The safety-fund banks, on the other hand, retained full control of their capital, except the small contribution

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made annually to the fund. They were free, therefore, to use both their capital and their credit in their discount business. Consequently the note-issue business was more profitable for the safety-fund banks.

In the one class of banks the notes were based upon securities purchased or possessed for that purpose, and the value of these securities was not always favorably connected with the demand for more bank notes. It might easily happen, and did happen, that when there was need for more currency it was to the interest of the banks to withdraw securities and sell them in the market, thereby decreasing their circulation and increasing their reserves. In times of pressure the withdrawal of securities was often the only way a bank could meet the demands for redemption of its notes. This happened during the panic of 1857. The report of the bank department in 1858 states that in September of 1857 the pressure upon the country banks to redeem their notes was beyond all precedent. Many of the interior bankers began to withdraw securities from the bank department by returning their circulation. It seemed the only way for these banks to meet the demand for redemption, since the capital of many of these small banks was mainly invested in the securities in the bank department. The total amount of stocks, bonds, and mortgages returned to the banks by the department from October 1 to 13, 1837, was \$2,641,422, mostly to country banks.^a

By elasticity of bank-note issues we mean that the amount of notes expands when there is demand for more

^a Assem. Doc. 4, 1858, Vol. I, pp. 14-16.

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currency for legitimate purposes of trade and that the amount contracts when there is no longer a demand. The operation we have just described was a perverse elasticity.

Experience has shown that there is much greater demand for currency at one season of the year than at another. This means that at one season the currency ought to expand and at another contract. But for the banks to create a new investment demand for securities would mean a rise in price to some extent at least, and the opposite if securities were withdrawn as a basis for notes and thrown upon the market suddenly. Increase of currency by the free banks, therefore, was ordinarily limited to such as could be obtained by the deposit of whatever securities the bank happened to have. The possession of securities involved the tendency to keep them on deposit at the bank department and to keep out the full amount of currency even when there was little demand, or, rather, as is apt to be the case under the currency principle of note issue, to calculate about how much currency could be kept constantly in circulation and then deposit securities for that amount. This plan prevented the possible losses connected with trying to expand or contract the notes to suit the needs of trade. If the bank should tie up its capital in securities to an amount greater than the circulation which it could keep out, it would mean that the part of the investment above the amount of notes would yield only the interest on the securities and nothing more. Therefore, there was little margin left for emergency, suffering resulted in time of stress, and panics were promoted under such a system.

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There was no certainty that when the business community was most in need of additional currency it would be accommodated.

On the other hand, the safety-fund banks based their notes on the general resources or assets of the bank, retaining control over their capital and being limited only as to the maximum amount which they might issue. They followed what is called the banking principle of note issue.^a It was not necessary for the safety-fund banks to tie up their capital in securities or cause delay in meeting the demands for notes. They could respond immediately and in exact proportion to the demands of trade. We have seen that these banks sometimes abused their privileges, and did not always issue notes based upon actual business paper, but sometimes upon accommodation paper. This was, however, not the fault of the asset principle of currency, but was the result of bad banking practice. This system is the one followed in German banking, where one-third of the issue of notes is secured by a cash reserve and the other two-thirds by short-time commercial paper of undoubted soundness. In the days of the safety-fund system in New York State the idea of such a cash reserve had not yet developed. This system of note issue means that when there are abundant general assets in the shape of good business paper, and consequently the demand is lively for currency, notes will be issued, and when business is not so active the notes will be automatically withdrawn without loss or disturbance.

^a White: *Money and Banking*, 3d ed., pp. 297-298 for distinction between "currency" and "banking" principle of note issue.

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Fortunately for comparison, we have the two systems existing side by side in New York State from 1838 to 1866. I have selected 25 free and 25 safety-fund banks, with about the same amount of capital in the aggregate. Five were selected from the city of New York and 20 from outside in each class, because the note issue of the country banks was a more important element of their banking business. The figures were taken from the quarterly reports of the banks to the comptroller during the years 1848, 1849, 1850, and 1851. It seemed necessary to take a period at least thus far removed from the beginning of the free-banking system in order that it might be found in a more perfect operation, and yet not too late in order that the safety-fund system might not be too near expiration. The accompanying diagram shows the results. No attempt is made to show the circulation in per cent of capital. Each group of 25 banks has about the same capital, but of course the free banks never issued so large a per cent of their capital in notes as the safety-fund banks. All that the diagram attempts to show is the actual variation in amount of notes issued by the two classes of banks with the same capital. The less elasticity of the free banks is thus shown. The June variation is large in both systems, due to the usual lack of demand for currency at that season of the year. The extreme range of variation of the safety-fund group was 536 thousands and the greatest single variation from one report until another was 475 thousands; in the free-bank group the extreme range was 290 thousands and the greatest single variation was 282 thousands. Thus, with a given employment of

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bank capital, the capacity of the two systems to issue and vary the amount of the issue from time to time is shown.^a

Mr. Root, in *Sound Currency*, Volume II, No. 5, page 22, has given a diagram showing the elasticity of the note issues of the safety fund and free banks, compared as a whole, and also of the rural safety fund and the rural free banks, when compared in groups separate from city banks. He has computed the issues in per cent of the capital, and his diagram is for a later period, 1858, 1859, 1860, and 1861. The results are more striking than in the diagram just presented, and show clearly the advantage of the safety-fund banks in elasticity. The decreasing use of bank notes as well as the inelasticity under the free banking system would surely have proved more serious than it actually was had not the safety-fund system been in operation at the same time and had not the deposit business been rapidly developing to take the place of notes.

Under the safety-fund system up to 1840 there was no law requiring redemption except at the bank's own counter. A safety-fund bank was not permitted to purchase its own notes at a discount. The notes of country banks were often at considerable discount in the city. They were purchased and sent home for redemption by brokers or bankers who made a business of thus securing the redemption of notes at a more or less unreasonable profit to themselves. The public which used the notes was thus made

^a The largest amount of notes issued during these years by the 25 safety-fund banks was 4,957 thousands, as compared with 3,548 thousands for the free-bank group. So, incidentally, the figures show that, under the law of 1838, note issue was less profitable and a much less percentage of capital was issued in notes.

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to bear the expense of redemption. This became a heavy burden. The banks made the profit out of the privilege of note issue and yet objected to bearing the expenses of redemption.

There had been much discussion in the legislature from the beginning of the safety-fund system about requiring redemption in New York and Albany at par, thus relieving the note holders from the great inconvenience and expense. This is now recognized everywhere as a necessary part of a currency system, but at that time the influence of the banks was strong enough to prevent the requirement. During 1837 the banks, during suspension of specie payments, had a mutual arrangement between city and country by which the bills of country banks were kept at par and the expenses of redemption were shared. This voluntary arrangement broke down in 1838 and 1839, when the free banks were being organized and specie payments had been resumed. Many of the free banks, as we described before, made a business of shaving notes and were allowed to purchase their own notes at a discount as well as those of the safety-fund banks. The notes of country banks were at a great discount in the city during 1839, even as much as 6 per cent. The situation became intolerable. The problem was taken up in the legislature in 1840. Some argued that to require the banks to bear the expense of redemption at par was only reasonable, since they made the profits. The debate shows that some thought the rate of discount ought to be graded according to the distance of the bank from New York City, since the actual expense of redemption would thus vary. The house adopted the principle of par redemption once in the

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course of the debate on the bill.^a The senate, however, would not agree. It seems that the legislature saw the need of preventing the evils in brokerage and "shaving" notes in New York City, but that the bank interests were unwilling to bear the whole cost of redemption. The bill was finally passed in May, 1840, requiring banks to establish agencies for redemption in New York or Albany, and fixing one-half per cent as the maximum discount allowed. This was a compromise between those who wished par redemption and the banking interests. The attempt was made to place the rate at one-fourth per cent when the notes were redeemed at Albany, since the cost would be less, but the rate of one-half per cent was finally agreed to as a concession to some of the country banks.^b

Still some free banks, not really banks of deposit and discount, made their profits buying up notes at one-half per cent discount. The senate committee on banks in 1850 reported on this situation. The governor's message was referred to by them as recommending further legislation to prevent "abuse in the organization, under the general law, of institutions designed rather to profit from the mere issue of notes than to furnish banking facilities to the business community."^c The committee agreed with the governor and they pointed out that the law allowing the purchase of notes at one-half per cent discount made such business a source of profit to many banks rather than the legitimate banking business. They

^a *Semiweekly Argus*, Apr. 3, 1840.

^b For debates see *Semiweekly Argus*, Mar. 17 and Apr. 28, 1840. For text of bill see *Semiweekly Argus*, May 5, 1840.

^c S. Doc. 25, 1850, Vol. I, p. 1.

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estimated that there was a circulation of \$8,000,000 in notes which were not at par in New York or Albany and on which, therefore, the one-half per cent might be charged. These notes were redeemed, according to the committee, about four times each year. This would allow the charge of one-half per cent on \$32,000,000 of notes annually. The committee pointed out 25 free banks with a capital of \$1,600,000 whose discounts aggregated only \$80,000, and individual deposits \$50,000. These banks were making their profits from issue of notes and buying their own notes at a discount of one-half per cent, only to issue them again. Ten of these banks showed a circulation of \$650,000 without any discounted paper. These facts led the committee to favor the reduction of the rate of discount allowed by law to the point where expenses of redemption would be just covered. This would drive such banks, as above described, out of business. Therefore, in 1851, the legislature provided that agencies must be established at New York, Albany, or Troy, and that the rate must not be more than one-fourth per cent discount. Still the public must help bear the burden which should have been carried by the banks, but at least the old evils were removed, and the charge reduced to about the actual expense involved in the transmission of notes home for redemption.^a Prompt redemption helped to inspire confidence in the banks. This law applied equally to both free and safety-fund banks.

^a S. Doc. 25, 1850, Vol. I, pp. 1-5, for details of above report.

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4. HOW THE CHARGES UPON THE FUND MIGHT HAVE BEEN DECREASED IF THE AMENDMENTS TO THE ACT HAD BEEN INCORPORATED IN THE ORIGINAL ACT.

We have already given evidence to indicate that those who passed the original act, and even bankers themselves, little realized the significance of making the bank fund responsible for notes and all other debts. The New York City banks objected to the fund because they must pay the assessment on their large capitals, while their circulation, for which they considered the safety fund as security, was relatively small. The country banks, on the other hand, paid their assessment on small capitals, while their circulation was relatively large. If deposits had been considered by the city banks as guaranteed by the fund, which was really the fact, the disparity between the city and country banks would not have been great. To-day, when a bank lends, not simply the money actually left in its charge by depositors, but its credit in the shape of deposit credit accounts on the basis of a sufficient cash reserve, this guaranty of deposits would be a matter of great importance, for it would increase the credit of the institution to have the borrowing public know that all deposits, whether of cash or credit accounts, were guaranteed by a safety fund, backed by all the banks.

The legislature in 1829, as shown by the debates, was considering the guaranty for notes, not other debts. Deposits were not a large enough element in the banking business to attract attention. The chief losses of the past had, at that time, been suffered by note holders. It was recognized that notes must be made a universal currency

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in order to be most useful. Deposits, while they are the same in essence as notes, need not nor can they become a universal currency. The comptroller, in his report in 1849, declared: "The State is under no more obligation to attempt this impossibility (i. e., to secure against all losses) than it would be the equally absurd one of making every merchant capable of meeting all the obligations he should incur." The duty of the State, therefore, begins and ends with furnishing "a good and safe currency for the public."^a In 1850 the comptroller expressed his opinion that the fund would have been "sufficient to fulfill the original design of insuring the redemption of the bank-note circulation," but it came to destruction because "all the liabilities of the banks, however illegitimate or extraordinary, were made chargeable upon it."^b In the opinion of the comptroller, this guaranty gave an unnatural credit "to unsound and speculative institutions, which enabled them to expand their affairs to an inordinate extent without reference to their intrinsic resources." Mr. Knox holds the same opinion, adding that the debts were contracted in some cases "for the emolument of their (the banks') managers."^c He holds further that the failure of the safety fund was due, not to principle, but chiefly to the attempt to charge it with all debts. The history of the fund from 1829-1866 indicates that if it had been applied to notes only it would have been ample, and "would have made the circulation of the safety-fund banks more secure than that of the banks under the free banking system"

^a Assem. Doc. 5, 1849, Vol. I, p. 53.

^b Assem. Doc. 8, 1850, Vol. I, p. 57.

^c Knox, p. 409 et seq.

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(p. 413). There was much discussion in the constitutional convention, in 1846, as to the obligation of the State to protect both bill holders and depositors. Some held that they should be considered on a par; others that the depositor should be left to take care of himself, being a "voluntary creditor," while the note holder is an "involuntary creditor" of the bank and, therefore, should be specially protected.^a

Whatever the theoretical merits of the case may be, the practical situation of a bankrupt safety fund confronted the legislature in 1842. In the act passed April 12, 1842, it was provided that the fund, after paying all the liabilities already incurred by bank failures, should be applied only to the payment of notes.^b Thus the legislature recognized the failure of the fund to secure all the debts of banks. The legislature, in 1838, when it passed the general banking law, made no attempt to secure anything besides notes.

What of the assertion that the fund would have been ample to meet the redemption of notes alone? This is a mere question of fact to be determined from the comptroller's reports. In his report for 1849 the comptroller stated that the banks had contributed to the fund since 1829 a total of \$1,876,063.76. The whole circulation redeemed for insolvent banks up to that time was \$1,548,558.33. This left a surplus of \$327,505.43 to redeem any other notes of failed banks, if the fund had been liable from the beginning for notes only.^c The comptroller, therefore,

^a *Semiweekly Argus*, Oct. 2, 1846.

^b For text of act in full see *Semiweekly Argus*, Apr. 29, 1842.

^c *Assem. Doc.* 5, 1849, Vol. I, p. 29 et seq.

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concludes that the fund would have proved an ample indemnity to the bill holder. It will be remembered, from the table of payments from the fund, before presented, that the total amount of notes redeemed from the fund was a little more than \$1,600,000.

If the comptroller had been given power in 1840 to call upon the banks for additional contributions as soon as the fund was diminished by the payments to redeem the notes of the City Bank of Buffalo, which failed during that year and whose notes were promptly redeemed to the amount of over \$300,000, it would have added, at one-half per cent on capital, over \$150,000 to the available bank fund in January, 1841. The contributions actually amounted to about \$914,000 at that date, because it was not until January, 1842, that the solvent banks began their additional contributions.^a In a statement issued from the comptroller's office, July 13, 1842, it was stated that the total contributions to the fund to April 1, 1842, had been \$1,069,143.48; also that there had been paid to redeem notes up to that date \$918,949.^b The amount for notes up to September 30, 1842, is given in the report for 1843 as \$952,785.^c If the legislature had done as suggested above, the total contributions, instead of being \$1,069,143.48, would have been about \$150,000 larger. Then, in 1842, the solvent banks were permitted to pay their future contributions in advance in the notes of the failed banks, for four, five, or six years, as explained before. This lightened the immediate payments in cash

^a Assem. Doc. 15, 1842, Vol. I, p. 34.

^b Semiweekly Argus, July 19, 1842.

^c Assem. Doc. 10, 1843, Vol. I, pp. 47-48.

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from the fund to the amount of almost \$500,000 and spread the burden of redemption of that amount of notes over a period of years, when the contributions of the banks would have come due. The whole amount of bills finally redeemed from the fund, it will be remembered, was a little more than \$1,600,000. When the banks had paid in the bills of the insolvent banks to the amount of almost \$500,000, on which they received 7 per cent interest until their regular contributions would have come due, there remained only a little more than \$1,100,000 in general circulation, which could have been promptly redeemed out of the funds on hand from previous contributions.

But the charges, even for notes, upon the fund would have been decreased if, when the law of 1829 was passed, provision had been made for the registration of all notes issued in the office of the comptroller. By this method fraudulent overissues would have been prevented. In discussing the causes of failure of the Buffalo banks we have already alluded to the discovery of illegal issues. These became a charge upon the fund and had to be redeemed along with the other notes. As shown by the table of payments for notes, before presented, there were redeemed \$317,107 in notes of the City Bank of Buffalo. Now this bank was permitted under the law of 1837, having a capital of \$400,000, to issue \$300,000 in notes. Therefore the comptroller actually redeemed \$17,107 of the notes of the City Bank in excess of the legal limit. He redeemed \$435,540 in notes of the Bank of Buffalo, whose capital was \$200,000, and whose legal limit of issue was, therefore, \$200,000. Here was an illegal issue of \$235,540. The total illegal issues of these two Buffalo

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banks amounted to \$252,647, which became a charge upon the fund. In April, 1843, to guard against more overissues, an act was passed providing for the substitution of notes registered and countersigned by the comptroller for the hitherto unrecorded issues, and after this date all new notes issued must come to the banks through the comptroller's office. If this amendment had been adopted in 1829, as was actually recommended in the debate, it would have reduced the charges upon the fund \$252,647, and that, too, at the beginning of the period of serious failures, for these two banks failed during 1840 and 1841.

Still other changes were introduced in the constitution of 1846, which, if operative from the beginning, would have still further reduced the burden upon the safety fund. Two provisions incorporated in the new constitution were:

(a) Individual liability of stockholders, after January 1, 1850, for debts of banks contracted after that date, to the amount of their stock. This is the same as found in our banking law to-day.

(b) The first claim of notes upon the assets of an insolvent bank. This, too, is a part of the modern Canadian safety-fund system.^a

If the failures which occurred during 1840-1842 had been settled under these provisions, and if the fund had also been liable for notes only, the charges upon the safety fund would have been greatly decreased. The table, showing the assets of the failed banks and the amount

^a The provisions constitute sec. 7 and sec. 8 of Article VIII in the constitution of 1846 of New York State.

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realized up to 1845, indicates that the assets of the Commercial Bank of New York would have much more than paid the note holders. This bank, as well as the Lafayette Bank and the Bank of Oswego, which paid their creditors out of their own resources, might, therefore, under section 8 of the constitution of 1846, be excluded because their notes could not have become a charge upon the fund. The eight other failed banks did not realize enough from their assets to pay the note holders alone. In 1845 these banks had realized, as calculated from the same table, almost \$700,000 from their assets. After this date the remaining assets of these same banks yielded about \$130,000, if the payments into the bank fund are a correct index of the amount realized. These receipts into the bank fund from the assets will be found in the table showing the charges against the fund for notes and other debts. So the entire amount realized from the assets of these eight banks was over \$800,000. All of these assets would have been applied to note redemption under the constitution of 1846. So Mr. Root estimates this as the decrease in actual charges upon the fund if notes had been a first lien on assets since 1829 and the fund only liable for notes.^a By actual charges we mean the amount which we have estimated as the total redemptions of notes from the fund on account of the insolvent banks—i. e., over \$1,600,000. We should exclude from this amount the circulation of the Commercial Bank of New York, \$139,837, because, under the constitution of 1846, this would have been more than redeemed from assets. The actual burden on the fund

^a Sound Currency, Vol. II, No. 5, p. 15.

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from the eight banks, therefore, was about \$1,460,000 for notes. If we diminish this by the aggregate assets, over \$800,000, we arrive at an estimate of the burden upon the fund of about \$650,000, provided notes had been a first claim on assets. This estimate agrees essentially with the figures of the report of the monetary commission of the Indianapolis convention, page 240 (footnote). The correctness of this estimate of course depends upon whether the receivers of the failed banks devoted any considerable part of the amount realized from assets to the settlement of the claims of note holders directly while the bulk of the notes were being redeemed from the fund. From the reports of the amounts redeemed from the fund this seems quite unlikely.

If the individual liability of stockholders to the amount of their stock had been in operation when the serious failures occurred, the claims upon the fund would have been still further reduced; how much could be only a guess.

If the hypothecation of notes as security for loans had been prohibited and prevented from the first, as was attempted after the serious failures, the circulation of some of the banks would not have been so large, and the claims upon the fund would have been less. The policy of an embarrassed bank would not have been so reckless, and the temptation to overissue notes would not have been so great.

After the serious failures the quarterly reports were required to state separately the loans and discounts to directors. If this had been required always, it might have restrained many of the large individual loans on poor security, and the loans for speculative purposes to some

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extent, all of which was so dangerous to the solvency of the banks.

It is evident that if all the amendments had been adopted in 1829 which were finally made to perfect the safety-fund law the burden upon the fund would have been greatly decreased. In the first place, over \$1,088,000, applied to other debts than notes, would not have become a charge upon the fund during the period when eleven banks failed, 1840-1842. From the \$1,600,000, actually paid to redeem notes of insolvent banks which failed during this period, the provision for registration of notes in the comptroller's office, would have deducted over 250,000, by preventing this amount of overissue. If the notes had been made a first claim on the assets of a failed bank and our estimate is correct, the charge upon the fund would have been further decreased by about \$800,000. Stockholders' liability, enforced after January, 1850, would still further have reduced the liability of the bank fund. The issue of almost \$1,000,000 in state 6 per cent stock would not have been necessary, and thus almost \$500,000 in interest charges would have been saved. Assuming all these provisions in operation from the first, the final charge upon the fund would have been probably less than \$500,000 on account of the failures of the period 1840-1842. There were several failures later, during 1854 and 1857, but the fund would have taken care of these without difficulty. The comptroller could have met all claims for notes promptly, and there would have been no depreciation of notes. The fund would have afforded ample security for notes, and, instead of being mortgaged during the remain-

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der of its existence to the full extent of the one-half of 1 per cent annual contributions, would have been security for the notes of banks which failed after 1842. Further, the annual assessment to keep the fund good would probably not have averaged over one-fourth of 1 per cent on capital, over the whole period from 1829-1866. This estimate agrees with that of Mr. Root.^a The Indianapolis monetary commission of 1898 estimated the average annual assessment necessary to meet the charges under the above conditions as less than one-tenth of 1 per cent on capital.^b This much is certain that the original one-half of 1 per cent assessment on capital would have been more than sufficient.

5. OPERATION OF THE SAFETY-FUND SYSTEM 1843-1866.

FAILURES IN 1848, 1854, AND 1857.

The bank fund was mortgaged to the full extent of the contributions until the charges incurred by the serious failures of 1840-1842 should be paid by the redemption of the 6 per cent state stock, issued to secure the immediate funds, under the law of 1845. Therefore the creditors of safety-fund banks, which failed after 1842, could not depend upon the fund for the redemption of notes or the payment of other debts. After 1843 the fund was responsible for notes only. If a bank failed and the note holders waited until the state stock had been all redeemed, and if a surplus then remained after the settlement of these prior claims, then the notes of the failed bank might be re-

^a Sound Currency, Vol. II, No. 5, p. 15.

^b See Report, p. 242.

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deemed from this surplus. It is clear, therefore, that after 1842, the assets of a safety-fund bank were the only available security against losses to its creditors. It is true that notes had been made a first claim on these assets in 1846, and after January, 1850, stockholders were liable, for debts contracted after that date, to the amount of their shares.

The first bank to fail, after 1842, was the Canal Bank of Albany, in July, 1848. Its capital was \$300,000 and its outstanding circulation at the time of failure was \$185,531.^a The comptroller in his report goes on to say that the bank had been illegally conducted and that the quarterly reports had probably been false. The new constitution had made the notes a first claim, so that the receiver was able to redeem the notes of the bank promptly from its assets. The safety-fund did not enter into the transactions at all.

We shall examine the reports of the receiver, however, to find out the sort of assets possessed and the kind of banking done. In 1849 the receiver reported the amount of assets as \$1,071,000 when he took charge July 17, 1848. A large amount had been collected.^b In another report he stated that Edwin Croswell alone owed \$163,744, on which he had paid \$201, and \$20,000 in securities. The Albany Glass Company owed the bank \$115,824, and had paid \$9,132.^c It appears from the reports that the bank held much "accommodation paper" and had made too large loans to individuals, often on poor security.

The same was shown for the Watervliet Bank when the receiver made his final report in 1849.^d This Watervliet

^a Assem. Doc. 5, 1849, Vol. I, p. 35.

^b Assem. Doc. 222, 1849, Vol. V, p. 2.

^c Assem. Doc. 185, 1849, Vol. III, pp. 4-5.

^d Assem. Doc. 227, 1849, Vol. V.

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Bank, it will be remembered, failed in 1842, but its affairs were very slowly settled. An examination of the records in the Court of Appeals at Albany showed that there were many suits for recovery by the bank of Watervliet against individuals who had given poor security, in mortgages or their own personal security, which proved worthless.

A select committee of the senate examined into the affairs of the Canal Bank. They reported that the facts at failure showed "neglect of duty, gross mismanagement, and the violation of several statutes."^a The affairs of the bank had been entrusted largely to the cashier. When, in 1839, a committee of directors examined the bank and recommended to the board certain changes, intended to check the discretion of the cashier, the cashier and his friends took active steps to eliminate from the board two members of this committee at the next election of directors, in 1840. August 3, 1842, a resolution was passed by the directors "that our cashier be, and he is hereby, authorized to purchase in his individual capacity, for himself and such other members of the board as may wish to participate therein, the stock of this bank to the amount of \$60,000, and to loan to the parties on their individual security the cost of the same."^b This purchase of stock seems to be connected with the purpose of the cashier and his friends to control the board of directors. In May, 1846, the cashier was authorized "to get rediscounted any paper belonging to the bank." This showed that the resources of the bank were greatly weakened. October 2, 1847, the cashier was authorized to loan E. N. Pratt \$51,000 when

^a S. Doc. 63, 1849, Vol. II, p. 2 et seq.

^b *Ibid.*, p. 4.

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the bank was in a desperate condition, and the cashier certainly knew it. The bank for some time previous to failure settled its daily balances with other banks, not by drafts on New York, as was the usual method, but by using almost the last penny of deposits gathered in during the day from the confiding depositors.^a

Some items of the \$1,071,000 assets at failure are interesting:

Bills receivable (much of it worthless).....	\$780, 782
Stocks, bonds, mortgages, and Watervliet certificate.....	97, 091
Cash in bills and specie.....	2, 192

The last item is absurdly small.

There was due to—

Stockholders.....	300, 000
Depositors.....	196, 294
Other banks.....	467, 910
Note holders.....	192, 486

The committee found that from the debts due to the bank, already settled by the receiver, the bank had lost \$109,074, and that \$364,547 of the assets were considered bad at present and \$222,538 doubtful, making a total very probable loss of \$696,159 out of the \$1,071,000 assets. Out of the balance the circulation must be paid first.^b

The cause of failure that appeared most prominent was the secret appropriation of funds by the cashier for his own uses, and his assent to large and irregular loans to directors without adequate security. The directors were not diligent and their confidence was abused, where they were not themselves guilty of misconduct. Frauds were concealed by false entries and oaths. There was a "Pratt

^a S. Doc. 63, 1849, Vol. II, pp. 5-6.

^b Ibid., pp. 7-8.

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Bank special account" carried for the purpose of concealing the operations of the cashier (p. 16).

J. K. Paige was made director in 1841 and president of the bank in 1843. At the failure he was indebted to the bank as principal to the amount of \$5,000, as surety for \$93,497, and overdrafts \$542. He was also president of the Albany Glass Company, whose paper the bank held to the amount of \$103,762, on which Mr. Paige was indorser for \$59,000. The effects of this company will not yield over \$10,000.

Edwin Crosswell was one of the commissioners to distribute the stock of the bank and one of its first directors. "His liabilities were very large, exceeding the amount allowed by law to all the directors of the bank," one-third of capital (pp. 12, 13).

Theodore Olcott was the cashier and was most to blame for the failure. At the time of insolvency, his liability to the bank as principal was \$59,006; for overdrafts, \$16,625, and as indorser for \$107,103, making a total of \$182,734. Only \$55,880 of this amount appeared on the books of the bank. His acts constituted fraudulent embezzlement.^a The design seemed to be deliberate to ruin the bank. I have given these details to show what sort of banking was still practiced.

The next safety-fund bank to fail was the Lewis County Bank, in November, 1854. The immediate cause of action was the failure to redeem its notes. It was almost purely a bank of issue. Its capital was \$100,000, and therefore

^a S. Doc. 63, 1849, Vol. II, pp. 9-19 for details of above.

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it was authorized to issue \$150,000 in notes. The special agent, appointed to report on the bank's condition, reported as follows:

Specie.....	\$2
Bills receivable.....	105,488
Stanton and Wilcox debt.....	117,371
Real estate.....	400
Overdrafts.....	159
Property.....	100
Total resources.....	<u>223,520</u>
Capital.....	100,000
Profits.....	11,689
Circulation.....	<u>125,283</u>
Total liabilities.....	236,972

The agent reported that the total debt of Stanton & Wilcox to the bank was \$221,310, which constituted almost the entire assets of the bank. The only creditors of the bank except its stockholders at the time of failure were evidently the note holders. The last quarterly report did not reveal the true condition of the bank, as shown by a later examination of the books for that date. Design in the false items was shown beyond a doubt. The examination showed fraud and collusion.^a

It was evident that this bank could not pay its note holders, but the safety fund was not available until about twelve years later, when the state stock had been paid and there was a surplus. Then an arrangement was made to redeem out of this surplus any bills of the Lewis County Bank still outstanding. The notes depreciated and before the fund became available most of them had disappeared. This failure, therefore, brought considerable

^a Assem. Doc. 10, 1855, Vol. I, pp. 110-135, for above details.

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loss to the public, and there was no adequate security offered by the fund.

During the panic of 1857 three more banks, under the safety-fund law, failed, as follows:^a

	Capital.	Authorized circulation.	Circulation at failure.
Bank of Orleans.....	\$200,000	\$200,000	\$200,000
Reciprocity.....	200,000	200,000	159,577
Yates County.....	100,000	150,000	148,958

The assets, together with the stockholders' liability, were sufficient to redeem a much larger proportion of the notes of these banks than of the Lewis County Bank. The bank department, in its report ^b for 1867, gave the outstanding circulation of the insolvent banks as follows:

Bank of Orleans.....	\$10,188
Lewis County.....	105,211
Reciprocity.....	12,766
Yates County.....	23,322
Total.....	151,487

From the above statement it appears how complete had been the losses of the bill holders of the Lewis County Bank. At failure the outstanding notes were given by the special agent as \$125,283, as stated before, while in 1866 there were still unredeemed \$105,211. Evidently the assets of the bank were worthless. The circulation of the three banks which failed last, however, had been reduced to a comparatively small amount by 1866. No doubt there had been considerable loss to note holders by depreciation and waiting for the affairs of the insolvent

^a Assem. Doc. 3, 1860 Vol. I, Table 4, in Appendix.

^b Assem. Doc. 4, 1867, Vol. I, p. 40.

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banks to be settled. This would have been prevented if the safety fund had been available to redeem the notes at once and reimburse itself from the assets.

FINAL DISPOSITION OF THE SAFETY FUND.

The bank department reported to the senate in 1866 that the last contributions had now been made to the safety fund by the solvent banks, since their charters all expired in that year. All claims upon the fund had been paid and there was a surplus of \$88,048. This surplus should be applied to the redemption of the notes of the banks that had failed since 1842. But it was for the legislature to decide how it should be applied. The superintendent of the banking department recommended that it be applied in equal ratio to the notes of the four banks.^a The legislature of 1866 authorized the bank department to convert the assets of the safety fund into cash and declare a dividend on the outstanding circulation of the four insolvent banks whose notes had not been fully paid.^b This was done and a dividend of 40 per cent declared. But so few of the bills still outstanding were presented that the superintendent was able to pay in full all that were presented for redemption. Many had been destroyed, probably because of the belief that they were worthless, especially of the Lewis County Bank, which had failed twelve years before.

After paying all the notes presented, there was still a surplus of \$13,144.19 in the fund. This balance was paid

^a S. Doc. 64, 1866, Vol. II, pp. 1-2.

^b Session Laws, 1866, chap. 564; also Assem. Doc. 4, 1867, Vol. I, p. vi.

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into the state treasury. Afterwards out of this sum \$3,959.75 was paid by authority of the legislature to the late Bank of Oswego "for interest upon an excess of its contributions to the bank fund, erroneously paid in 1842."^a Thus was closed the operations of the safety-fund system. It had furnished tardy and inadequate security for the notes of banks failing after 1842. This was due to the fact of its having been mortgaged during the early years of its existence, because of certain imperfections in the law itself which were later remedied. The experience of these later years in no sense condemns the principle involved in the completed law.

^a Assem. Doc. 7, 1867, Vol. I, p. 7.

CHAPTER IV.

THE GENERAL BANKING LAW OF 1838; CONCLUSIONS.

I. THE ADOPTION OF THE SECURITY-DEPOSIT SYSTEM UNDER A GENERAL BANKING LAW.

The safety-fund system was not abandoned because of its failure to provide the requisite security to the note holder. Before 1838, whenever it had been called upon, which had been the case in the redemption of the notes of five different institutions, it had proved entirely adequate. All advances made out of the fund to redeem the notes of these five banks either had been repaid to the fund or were being returned rapidly. Nothing had been finally lost on notes issued under the system during the first nine years of its existence. And yet, in 1838, another system was inaugurated and the method of special charters by legislative grant abandoned. What is the explanation for the change?

We have reviewed the abuses which were inevitable under a system of special charters. The securing of the charter through political influence and logrolling, the distribution of the bank stock as personal or political favors, the placing of the office of bank commissioner in the field of political spoils, all have been described, and it was these evils that brought the system into disrepute. Therefore the system was abandoned in 1838, and a general banking law enacted under which special charters were not granted, but individuals or associations having

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the required capital might do a banking business if they first deposited with the comptroller certain approved securities upon which notes might be issued.

Before 1838 banking was a monopoly, granted by legislative act. About this time there was a new faction developing, called the "Locofocos." They adopted a platform in which they declared their opposition to all monopolies granted by legislation, on the ground that they were violations of the equal rights of the people.^a With the aid of the Whigs, they carried the elections in New York City in the autumn of 1836 and the spring of 1837. In the legislature this idea of monopoly became a chief point of opposition to the safety-fund system. The free banking act of 1838 was the result. Thus was monopoly abolished from the banking business and the principle of note issue changed.

The debates in the legislature from 1836 until the law was finally adopted are interesting because they show the growing antimonopoly spirit and the gradual departure from the principles of the safety-fund law, which had seemed to give general satisfaction so far as its principles were concerned, to an entirely different principle of note issue and security.

From the first the restraining acts of 1804 and '18, previously described, had given dissatisfaction. To require special safeguards from banks issuing notes, which must pass current as money, seemed reasonable and logical to most at the time the law of 1829 was passed and even before this time. But to prohibit private banks of de-

^a Hammond: History of Political Parties, p. 493 et seq.

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posit and discount without special charters had seemed from the first a suppression of competition and an interference with the rights of private business and the employment of private capital.

The whole problem of private banking was the subject of a report to the senate in 1825.^a The report was upon a resolution in regard to banking. Whether restraints on private banking ought to be repealed was made to turn upon the question of public welfare. The report claimed that private banking would facilitate obtaining credit and do away with many of the evils which we have described as prevalent before the safety-fund law of 1829. It claimed further that there was nothing to rely upon for the good conduct of an incorporated bank but the honesty of the directors. This we have found painfully inadequate in actual practice. The report further pointed out that a body created by the legislature thereby secures a credit which enables it to circulate bills without question. The private bank would stand on its own record and those who owned and managed it would be personally liable for the debts they might create. This would promote prudence and caution. If this was not security enough for the public, the legislature might require bonds and mortgages to secure paper issued. The report closed with the distinct antimonopoly expression that if the restraints were removed, then "whatever advantages are to be derived from banking operations all citizens would be free to enjoy alike."

In 1826 the committee of the senate on banks made a report which contains much interesting material on prin-

^a Sen. journal, 1825, pp. 99-103.

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ciples of banking. They asserted that principles of banking "will not submit to the control of arbitrary direction" and advocated a standard of natural liberty (p. 10). Abuses arising from the frauds of officers and agents are fit and proper subjects of legislative interference; but evils ascribable to mismanagement, which result in speculation or extending discounts and circulation beyond the wants of trade, are of another character and "are perhaps entirely beyond the reach of direct legislation for correction" (pp. 14-15). These latter must be left largely to enlightened public sentiment and the practice of business men interested in fair and sound commercial policy. "Confidence, induced by the supposed sanctity of a charter, enables the unworthy and dishonest managers of its (a bank's) concerns to flood the country with a circulation far beyond what commercial credit would have effected" (p. 16). The committee further declared that this state of affairs would not exist to any great extent "if a monopoly, odious to the free spirit of our civil institutions, did not exist" (p. 19).^a These reports were before the adoption of the safety-fund system of banking. Much that was claimed in them has been shown to be true under the operation of the law of 1829.

The issue was again taken up with vigor during the session of 1836, when the repeal of the restraining law upon private banks of deposit and discount was debated. There appeared to be a general friendliness to the principle of a safety fund as a protection to the note holder, but

^a Report of the committee on banks and insurance companies on petitions, Albany, 1826, pp. 1-22.

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the opposition was concentrated upon the monopoly of the deposit and discount business. There had been a time when it was not dreamed that note issue could be separated from the deposit and discount business, or rather deposits were regarded as an insignificant part of the banking business. Now the deposit business was attaining considerable proportions, especially in the city. But the advocates of private banks of discount and deposit sought to adjust them to the existing safety-fund system. More than once in the debates the safety-fund system was declared to be the safest yet devised and satisfactory.

A letter in the Albany Argus, December 24, 1836, over the name "Franklin," but written by Mr. Flagg, declared that the existing law abridged fair business rights and discountenanced the free use of capital. The law of 1829 was, in his opinion, the outcome of selfishness and rivalry rather than for the public good. It was the age of monopoly. He advocated allowing banks of deposit and discount without the power of note issue, and favored a general law instead of special charters. Nothing was done at the session of 1836.

During the session of 1837 the antimonopoly feeling increased. The debates show still a friendly spirit toward the safety-fund system, but they advocate it under a general law. Gallatin, in the Argus, January 14, 1837, defended severe restrictions on the issue of paper money, but opposed restrictions on deposit and discount by private bankers. Competition was desirable. Depositors need no special protection since the transaction is en-

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tirely voluntary and the depositor exercises judgment as to where he shall place his confidence.

A report to the senate on the governor's message in 1837 pointed out that there was growing a popular sentiment against banks, due to abuses in the granting of charters. The committee considered it impolitic to grant to individuals the power of issuing bank notes, and commended the safety-fund system as the safer for note issue. They answered the objection that the system then in operation was a monopoly by saying that it was not a monopoly in an odious sense; that privilege was conferred upon a part for the benefit of only a part. Note issue and banking had been restricted for the protection and benefit of all. Any person with the capital might buy bank shares and thus participate in the profits of the investment. The committee concluded by commending the safety-fund system as better than any other that they could suggest.^a

The debate on the repeal of the restraining law against private banks of discount and deposit was opened early in January. Before the end of the month the senate agreed unanimously to the repeal. Early in February the house followed by passing the bill, with scarcely any opposition.^b

Now, the subject under discussion, after the problem of allowing private banks of deposit and discount had been disposed of, was a general banking law, to remedy the evils of special grants by charters. During this session

^a S. Doc. 38, 1837, Vol. I, pp. 1-13.

^b *Semiweekly Argus*, Feb. 3, 1837, gives vote in house. For text of the law see *Argus*, Feb. 3.

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of 1837 the discussion favored a general law which should retain the safety-fund principle. Public meetings over the State passed numerous resolutions to the same effect. They approved the safety-fund idea but urged the remedy for its defects by adopting a general law which would abandon the monopoly features of the old system.^a Local papers took up the discussion with vigor. One paper described the safety-fund system as the "noblest" ever devised, but advocated the abolition of the "odious" monopoly features.^b A communication in the *Argus* for March 21, under the title "The Times," declared "No man can point to a state or county convention, a town or village meeting, which has indicated the slightest wish to abandon the system (the safety fund) or to change any of its essential features." In the *Argus* for March 28, a correspondent from Seneca Falls writes of a convention of delegates from six counties at Geneva. Resolutions were adopted approving a general law on the plan of the safety fund. The western counties seemed especially urgent. Like meetings were recorded in the issue of the *Argus*, March 31, at Hudson, Auburn, Batavia, and Albion. The sentiment at these meetings favored the old system, as modified by desire to prevent monopoly and abuses.

The select committee of the senate on banking law recommended a system of private banking, not related at all to the safety-fund principle. They proposed unlimited personal liability, and a pledge of one and one-half times

^a Semiweekly *Argus*, Mar. 14, 1837, Rochester meeting.

^b Semiweekly *Argus*, Mar. 17, 1837. The *Argus* for Mar. 21, 1837, gives further extracts from many local papers in favor of a general safety-fund law.

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the capital in property, put under the care of trustees, for the benefit of creditors.^a When debate began in the senate, the house bill, which had incorporated the safety-fund principle, was offered as a substitute for the bill reported by the select committee. The debates seemed to recognize that public sentiment inclined toward the latter.^b The outcry was against monopoly in banking and yet the majority favored severe restrictions as to note issue. The tendency in Europe has been steadily toward centralization and monopoly in note issue. The real contest was for freedom in deposit and discount banking which is generally admitted to-day. The session of 1837 closed with the problem still under discussion.

When the legislature met in 1838 there was evident a change of sentiment as to the subject of a banking law. The Democrats were in power and were determined to inaugurate a system different from the one in operation. To do this they were forced into hostile opposition to the safety-fund system, partly from political motives.

But public sentiment also had evidently somewhat changed in its attitude toward the safety-fund system. The year 1837 was a time of investigation of banks. Several committees spent the whole session of the legislature in probing the affairs of the individual institutions. The charter of the Lockport Bank was repealed on account of violations of law. The Buffalo banks were under injunctions. Certain bad practices were discovered in a number of the banks by a special committee, as we have described in a previous chapter. The bank officers

^a *Semiweekly Argus*, Apr. 4, 1837; S. Doc. 55, 1837.

^b *Semiweekly Argus*, Apr. 7, 1837.

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were shown to be eager for profit at the expense of sound banking and regardless of the public interests to a shocking degree. The system of supervision by commissioners did not seem to work satisfactorily. The method of their appointment had been changed in 1837, so that all were appointed by the governor and senate, instead of two of them being appointed by the banks themselves, as in the original law. This change brought the office within the field of political spoils. There was growing in the minds of the people a distrust of the old system. It was a favorable time for political motives and selfish interests to accomplish their purposes. It was comparatively easy to ring the changes on the monopoly features of the old system, which appealed to all, and point to abuses which seemed to condemn even the principle of the safety fund.

Consequently, in the debates on the general law, in 1838, there was little attention to the safety-fund principle. The evils revealed by the investigations of the preceding session were emphasized and attributed to the monopoly features of the old system. In the report of a select committee to the assembly, the criticism was made that the law of 1829 created more banking facilities in one part of the State than another. The western part of the State was demanding more banks, as shown by the map in Chapter III. The legislature was slow to grant this section its demands, as the map indicates. Therefore, opposition was aroused, but chiefly against the monopoly system of granting charters and not against the principle of note security. Jealousies were aroused between different sections of the State. The committee felt that

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throwing the business of banking open "to all will give the bill holder the necessary security," and the jealousies now existing will be overcome, and capitalists will place their capital where it can most profitably be employed. Competition will afford the borrower adequate accommodations.^a

The blame for the inflated currency, during the years preceding the panic of 1837, was placed upon the monopoly system of banking. The evils of the panic were due to this inflated currency, in the opinion of many. Therefore the monopoly in banking must be abandoned in order to avoid future panics. The conclusion was logical, but the premise may not have been true. Speculation and overexpansion would probably have occurred under any system, and they did so occur in every part of the Union. It must be admitted that the safety-fund system stood the test of the panic year, 1837, remarkably well, and no serious failures occurred until the process of liquidation, following the panic, revealed the bad banking and worthless assets of previous transactions. Whether legislation and a different system could have prevented these is at least open to question. This much is known, that the free banking system, adopted in 1838, was not able to prevent serious losses upon securities deposited for notes until experience had taught officials what sort of securities were safe. It may be remarked also that the panic of 1857 came on with no less regularity than that of 1837. The panic of 1857 occurred after the system of free banking and bond deposit for notes was in full operation and

^aAssem. Doc. 122, 1838, Vol. III, for above report.

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after the safety-fund system had passed its zenith. It does not, therefore, seem correct to blame the safety-fund system or monopoly for panics, although some of the bad practices under that system did promote panics. Some of these evils were remedied by legislation and some could not be reached.

In the debate on the general law, in the house, on February 19, an amendment was offered subjecting banks to be formed under the law to safety-fund rules, but it was lost.^a The bill was amended finally so as to require each bank to keep 12½ per cent of the circulation in specie as a reserve for redemption of notes. The chief concern of the bill was to protect the note holder. No mention of a reserve against deposits was made in the debates. It was not yet recognized what part deposits might play in a panic. This was learned in 1857. The specie requirement was soon repealed.^b The speech of Mr. Griffin in the house on the bank bill asserted that the present banking law was contrary to our institutions and portrayed the benefits of competition. He declared that if a man should be denied a discount at the counter of an incorporated bank he could turn to others without falling into the hands of usurers if free banking should be established by the legislature.^c It had been revealed by the inquiry of 1837 that some bank officers had been guilty of refusing discounts and later lending the money at a usurious rate, on their own account. "No longer shall legislative aid be

^a Daily Argus, Feb. 20, 1838.

^b Daily Argus, Apr. 19, 1838, for facts as to specie reserve.

^c Daily Argus, Apr. 6, 1838.

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extended to make the rich richer and the poor poorer," exclaimed Mr. Griffin in the same speech.

The bill finally passed the house by a vote of 86 to 29.^a The senate adopted it with little change, except the requirement of a specie reserve of 15 per cent, which was later reduced to 12½ per cent by conference. Both senate and house refused to incorporate the principle of personal liability in the bill. The senate vote was 20 to 8.^b Under the new law, individuals or associations were authorized to engage in the business of banking, and to receive notes from the comptroller, registered and countersigned, provided they first deposited with him stocks of the United States, of the State of New York, or of any other State approved by the comptroller, or bonds and mortgages of a specific sort. By this general act each association was authorized to fix its own name, to determine the amount of its capital, provided always it had a paid-up capital of at least \$100,000, to fix the period of its existence, and to designate the place of operation. No special charter was required and no chance was given for "logrolling" in the legislature or favoritism in the distribution of bank stock.

In case of the failure of a bank to redeem its notes after a ten days' notice the comptroller was authorized to sell the securities and apply the proceeds to redemption. We have already compared the safety-fund and free banks in the preceding chapter as to the losses sustained by the bill holders of each during the early years of their operation. The difficulty at first was in selecting such securities as would prove good under pressure of a forced sale.

^a Daily Argus, Apr. 6, 1838.

^b Daily Argus, Apr. 18, 1838. See text of bill in Argus, Apr. 20.

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Bonds and mortgages and state stocks did not prove adequate when a bank failed and they must be disposed of on short notice. Therefore losses to bill holders occurred under the general law until these imperfections were amended. The comptroller, in his report for 1846, gives the amount of depreciation upon the securities of 29 insolvent free banks which had to be sold to redeem notes, up to 1846. These securities were state stocks and bonds and mortgages. New York state stocks averaged 88.5 per cent of their nominal value. The stock of other States ranged from 49 to 73 per cent. Bonds and mortgages averaged 70 per cent. This depreciation meant a loss to note holders.^a In the debates of the constitutional convention of 1846 one member referred to the fact that the safety-fund system had been in operation for sixteen years with 11 failures, while the free-banking system had been in operation for seven years with 29 failures. Each had about the same number of banks.^b

Thus was a new system of banking and note issue put in operation, partly from political motives, partly because there had developed a distrust of the existing system, due to certain evils connected with it, but mainly because there had grown up an intense opposition to monopoly grant of special privileges by legislative action which made it possible for those who had political motives and those who had selfish interests to point to the evils revealed in the old system and unite the opposition on the principle of monopoly and natural liberty as opposed to special privilege.

^a Assem. Doc. 25, 1846, Vol. I, Statement 16.

^b *Semiweekly Argus*, Oct. 2, 1846.

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2. CONCLUSIONS.

WHAT BEARING HAS THE OPERATION OF THE SAFETY-FUND SYSTEM, AS WE HAVE DESCRIBED IT, UPON THE GUARANTY OF DEPOSITS?

In the first place, it must be remembered that the fund in New York State proved inadequate for both notes and deposits. The speaker of the house in 1829 had declared it so, and had offered a substitute which provided for a larger fund, but his amendment was rejected. Few realized the fact that, as the years passed, the deposit business would rapidly increase and the relative importance of note issue diminish. When it was discovered that the other debts than notes of the banks that failed in 1840-1842 would require over \$1,000,000 from the fund after the application of all available assets, then the legislature hastened to relieve the fund from responsibility for deposits or any debts except notes. Therefore the safety fund was only a security for deposits during 1829-1842. After that date the fund was only meant to secure notes and did that very inadequately, because of the mortgage upon the fund already incurred from the responsibility for all the debts of banks failing during 1840-1842. The legislature did not discuss the question of guaranty of deposits when it made the change of law in 1842. It was confronted by a condition. Besides, the deposit business had not developed to the point where losses to depositors from failure of banks outweighed or even approached the losses to the public through bank notes of insolvent institutions.

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The following table^a will show the development of banking through the entire State. All banks, both free and safety-fund, are included, since it is the purpose to show the growth of capital in banking and the corresponding increases in deposits, circulation, and specie, with their relation to each other.

[Amounts are expressed in millions of dollars.]

Year.	Number of banks.	Capital.	Loans.	Deposits.	Notes.	Specie.
1836-----	86	31.3	72.5	19.1	21.1	6.2
1837-----	98	37.1	79.3	19.3	24.2	6.6
1838-----	95	36.6	61.0	15.7	12.4	4.1
1840-----	96	36.8	52.8	16.1	10.6	5.9
1843-----	137	43.4	61.5	27.4	17.2	11.5
1846-----	155	43.0	72.0	30.6	22.3	8.0
1849-----	192	45.5	90.2	38.2	24.2	8.1
1852-----	240	59.7	127.2	65.0	27.9	13.3
1853-----	280	79.0	145.9	78.1	32.6	14.1
1856-----	303	96.4	183.9	96.9	34.0	12.9
1857-----	311	107.5	170.8	83.5	27.1	14.3
1858-----	301	110.3	192.2	108.2	28.5	28.3
1860-----	306	111.8	200.1	116.2	31.8	21.7

From the above table it will be clear that between 1836 and 1860 the banking business had been rapidly changing in character. The banking capital increased very slowly up to 1850, and then with extreme rapidity up to the panic of 1857. It was another period of speculation. But the thing that appears most striking in this table is the great increase in deposits and the relative decrease in the use of bank notes. In 1840, when the serious failures of safety-fund banks were taking place, deposits amounted to 16.1 millions; in 1860 they had increased over seven-fold, while the capital had increased only threefold.

^a Bankers' Magazine (N. Y.), Vol. XI, 3d ser., March, 1877, p. 665.

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Circulation, on the other hand, had increased only three-fold from 1840 to 1860, or, since the circulation was very small in 1840, if we compare 1837 with 1860, the increase is less than 50 per cent, as compared with over 700 per cent for deposits and 300 per cent for capital. The specie held in the vaults had increased about fourfold, but when the great increase in demand obligations of depositors is considered, this increase was entirely inadequate. It only constituted in 1857, when the panic came on, about 13 per cent, or a little over one-eighth, of the combined obligations to depositors and note holders. That \$1 in specie should be considered sufficient basis for \$8 in notes and deposits was absurd. This amount, it will be remembered, was almost the exact amount of specie required in the law of 1838 against circulation alone. Evidently banks did not realize until the panic of 1857 that deposits now constituted the danger point in banking and must be covered by a reserve, as well as notes. In fact, the notes of the free banks were covered by securities, but the depositors depended upon the available resources of the bank for prompt payment. We are better prepared to understand the serious panic of 1857 after the examination of the table.

In 1858 the report of the banking department stated: "The error of the day has been in considering a specie basis of, say, one to eight or nine of immediate liabilities sufficient to sustain specie payments unless entire confidence was maintained between the debtor and creditor."^a The report goes on to say that the banks suspended because of the home demand for coin. "Experience, for

^a Assem. Doc. 4, 1858, Vol. I, p. 8.

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the first time, has shown the bankers of New York that there is such a thing as suspending specie payments from an internal demand for coin" (p. 14). The pressure caused large demands upon the country banks for redemption of their notes. Many of the free banks could only do this by withdrawing their securities from the banking department and returning their notes. They had no adequate reserve from which to redeem notes, and their capital was tied up in the securities deposited in the banking department. There arose a distrust among the banks themselves, and when a bank could not redeem all notes presented at once it was posted as suspended. By October there was a list of 30 such banks published as failed in the papers. The public took alarm, depositors started a run on banks, and suspension was inevitable, since the reserve was not adequate for both notes and deposits. The report goes on to say that such a state of things was new and had not been dreamed of by bankers themselves.^a The greatest danger to the banker, as well as to the public, lay in the large amount of his deposits, and the least in the currency he issued. This was a reversal of the situation in 1840-1842. The report claimed that the situation had been aggravated by the banks paying interest on demand deposits and country-bank balances. The same is often claimed to-day. This makes the banks borrowers as well as lenders and reverses the system of sound banking. The report condemned the practice as promoting speculation and curtailing bank-note issues. The report concluded by recommending that a 20 per cent specie reserve be required for deposits,

^a Assem. Doc. 4, 1858, Vol. I, pp. 17-18.

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but that the country banks outside of New York, Albany, and Troy be allowed to count as specie their balances in the redemption cities (p. 31).

The need had now become clear of in some manner protecting depositors. The report above quoted recommended that this be done by requiring a specie reserve of 20 per cent. Already the constitution of 1846 had provided for the personal liability of stockholders to the amount of their shares of stock. In our national banking system we require a specific minimum reserve and provide for several examinations of each bank through the year without warning, besides the liability of stockholders, detailed reports, and other restrictions to insure the solvency of the banks.

The question recurs as to why bank deposits should be guaranteed by a safety fund contributed to by all the banks. A report of the committee on banks and insurance companies of the senate of New York in 1849 referred to the note holders as "involuntary creditors" of a bank. They receive the bills that pass current as money, and for the most part can not discriminate between the good and the bad. Bank notes pass current more readily than checks because the bank is better known over a wider area, and the note is, therefore, more acceptable than a personal check; but its acceptability depends upon its security. The same report referred to depositors as voluntary creditors and therefore not in need of the same security against loss as the note holders.^a This was the trend of opinion at that period, but at that

^a Bankers' Mag. (N. Y.), vol. 3, May, 1849, p. 687.

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time deposits had not yet assumed their present importance and therefore the issue was not so urgent.

On the other hand it has been shown that if the law of 1829 had been from the first responsible only for notes and amended as it was after 1846, it would have been entirely adequate to protect the note holder. The assessments to keep it good would have been much less than they actually were. It might be said that the assessment should, logically, be levied on the average circulation rather than on capital, as was the case in New York State. It is so levied under the Canadian system, which operates successfully.

The safety-fund idea was adopted by other States than New York. In Ohio the branch system of banking was used. After the law of 1845 was passed, each branch was required to deposit with a central board of control 10 per cent of the amount of its notes in circulation, either in specie or in bonds of Ohio or the United States, as a protection for the note holders of any or all the branches. Each branch was liable for the notes, but not the general debts, of the other branches. In case of the failure of a bank to redeem its notes the board of control assessed the other branches pro rata to pay the note holders. The branches were reimbursed from the assets of the safety fund as soon as they could be converted into cash, and the fund, in turn, was reimbursed out of the assets of the failed bank before any other creditors were paid. The system worked successfully in Ohio as in several other States.^a It is to be noted that the size of the fund in this case was 10 per cent, and that it was levied

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upon the average circulation. This itself was somewhat of a check upon excessive circulation. In New York State the assessment on capital had no relation to the amount of notes issued and therefore did not afford this check. Besides, the method of levying upon capital excited the opposition of the city banks, which had large capitals and relatively small circulation, while the country banks had small capitals and relatively large circulation.

