

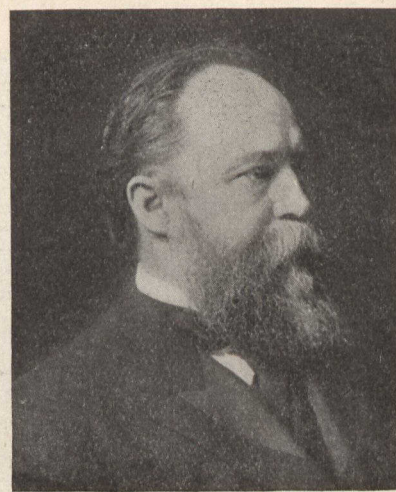
Sir Edward Clouston, Bart,
Vice-Pres. and Gen. Mgr Bank of Montreal.



Mr. Stuart Strathy,
General Manager of Trader's Bank.



Mr. D. R. Wilkie,
Pres. and Gen. Manager Imperial Bank.



Mr. B. E. Walker,
President Canadian Bank of Commerce.

INSPECTION OF CANADIAN BANKS

By Z. A. LASH, K.C.

WHEN a bank fails there is a general consensus of opinion among those who lose by the failure that somebody should have done something to prevent the failure, and that had a proper oversight of the bank's operations been exercised by the proper authorities, the failure would not have occurred.

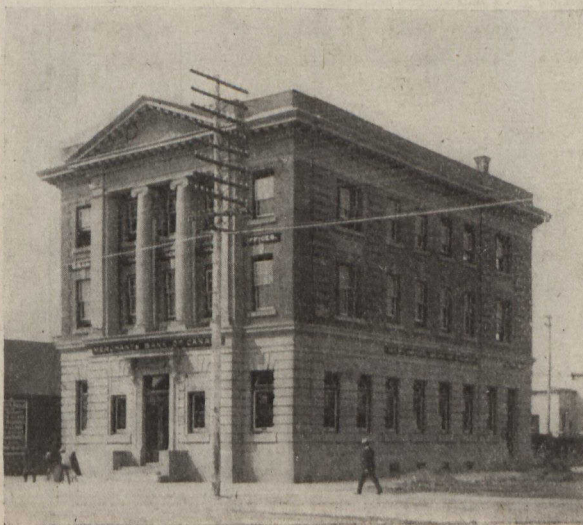
This opinion is not confined to those who lose by the failure; a general discussion takes place, ending in the conclusion that the government should do something to prevent a recurrence of the disaster. The precise something to be done is not stated very definitely but the opinion is expressed in general terms that there should be government inspection and that with such inspection the public and the shareholders would be protected.

If a plan could be devised whereby reliable information of the right kind respecting a bank's position could from time to time be obtained by some authority acting in the public interest, such authority having power to initiate action with respect to the bank should the public interest so demand, the banks themselves should heartily support such a plan. The difficulty is to decide upon the nature and extent of the information to be obtained and the means by which it should be obtained and the action (if any) to be taken when it has been obtained. My object is to throw some light upon these questions and to endeavour to help in their solution. The questions are eminently practical ones—theory aids but little. What would suit one set of conditions would not suit a different set, therefore it is necessary to consider what our conditions in Canada are before an intelligent answer to the questions can be given.

Although there are at present only twenty-nine banks in Canada in active business yet there are 2,214 branches of these banks doing business in 1,186 different cities and towns including the branches in London, England, the United States of America, Newfoundland, Jamaica, Cuba and Mexico. The branches on this continent extend from the Atlantic to the Pacific. Each branch is for practical purposes a separate bank, keeps a separate set of books, receives savings bank and general deposits and collects money for customers and correspondents; lends money by discounting bills and notes and by way of overdrawn accounts and on call, issues bank notes for circulation and carries on a general banking business with the public and with other banks and correspondents. If a branch has deposits in excess of its loans the surplus generally is sent to some branch where the loans exceed the deposits and for this and other reasons various branches have dealings with other branches as well as with head office. Each branch manager has, within certain limits, a discretion respecting the business of the branch, but each is, of course, subject to the general authority of the head office and keeps it continually informed of its business and position. This is done by returns on forms supplied for the purpose and by special reports and correspondence. By the Bank Act certain limitations are placed upon the powers of banks with respect to the investment of their moneys and to the nature of their loans and special provisions are made with regard to the kinds of securities which may be and may not be taken. Speaking generally, all credits and advances (except for trifling amounts and except call loans on high-classities) at the various branches are considered and passed upon by the head office before they are considered by the board of directors. This entails much correspondence with the head office, and sometimes personal visits of the branch manager. It would not be possible for the executive of a bank to properly carry on its business and discharge their duty with-

out some system whereby through others than the branch managers themselves the accounts and transactions of the various branches may be examined, audited, verified and reported upon and whereby it may be ascertained whether the instructions of the head office are being carried out and the duties of the branch manager and his staff are being properly performed. There are many things at a branch which require looking into other than the cash accounts and the verification of loans and securities, and for the reasons given below no government or outside examination audit or inspection would dispense with the examination audit and inspection by the banks themselves of their various branches. For this purpose each bank has a trained staff of inspectors continually visiting the branches and reporting thereon to head office. A short reference to some of the duties of the inspectors will give an idea of the magnitude of the work, and when it is borne in mind that this work has to be done at each branch at least once a year, and when it is remembered that the branches of our Canadian banks are 2,214 in number and that they extend over half a continent in addition to Newfoundland, Cuba, Jamaica, Mexico and Great Britain, the difficulty and expense of the task will be appreciated. What may be considered as the routine duties of the inspector and his assistants embrace the examination and verification of—

- (1) The accounts in the current accounts and savings bank ledgers and collection registers. These accounts are many thousands in number.
 - (2) The cash accounts and counting of cash and bank notes on hand.
 - (3) The bills and notes discounted or held for collection.
- This involves the examination of each bill and note to see that it is regularly made and endorsed. It also involves the examination of powers of attorney or authority of those who sign for companies or others. Also an examination of the diary in which the due dates of the bills and notes are entered and the checking of the entries therein.
- (4) The deposit receipts issued and the accounts respecting them.
 - (5) The liability ledger accounts.



A Typical Branch Bank Building—The Merchants Bank at Edmonton.

(6) The securities held at the branch. This involves an examination of the securities themselves and of the transfers or assignments, or hypothecations to the bank and of the authority of those signing for others. It also involves considering the regularity under the Bank Act of the taking of securities. The above are the main items embraced in the inspector's routine work but there are in addition numerous details which are of minor importance but which cannot be overlooked. 'Tis the chip which shows how the stream runs, and many an important result has followed the examination of a minor detail. Should any entry or transaction appear to be unusual it is the inspector's duty to get a full explanation of it. In addition to these, comparatively speaking, routine duties of the inspector, he has to perform a much more important and responsible task, one calling for high business ability and judgment and for an appreciation of the banking business in Canada which only long training under our system can supply. He is relied upon by head office for an independent opinion upon the general condition of the branch, the capabilities of the branch manager and staff to properly conduct its business, and specially the branch manager's skill and judgment in deciding upon credits and loans. He is also relied on for independent information and opinion respecting the individual accounts and credits and the wisdom or unwisdom displayed in connection with the opening or continuing of them. I have already said that speaking generally all credits and advances at the branches with certain exceptions are considered and passed upon by the head office. Notwithstanding this, the head office requires the inspector's opinion upon the position, and with this independent help the executive is better able to deal with any questions which may arise and to instruct the branch manager with respect thereto.

It is evident that no government or outside examination audit or inspection could take the place of the system of inspection established by the banks themselves. That system is a vital part of the very essence of the bank's business, viz., the lending of money and the management of their branches. It must go on no matter what outside plan of inspection is devised. The duplication of it or of any part of it would be an additional expense which the banks could not in justice be asked to bear. I am free to admit that the mere question of expense should not be allowed to stand in the way of the public interest if no other way to properly protect the public could be found. The questions here are whether an outside inspection of the kind established by the banks would be practicable and of any real use and would the enormous expense involved be justified by the results obtained?

Before endeavouring to answer these questions a consideration of the reasons why any inspection at all on behalf of the public is required will be helpful. It may be taken for granted that if no bank ever failed, and if no depositor ever lost his money there would be no occasion for public interference, the shareholders might be safely left to correct any abuse or mismanagement. The chief reason therefore why information respecting a bank's position should be obtained by some authority acting in the public interest is in order that such authority may interfere when necessary to prevent if possible a failure and loss to the depositor. This leads to a consideration of the causes for a bank's failure, because unless the cause can be prevented or removed the effect is sure to follow. It is safe to say that except in times of National crisis or disaster which no human foresight can prevent or provide