

The Bank Depositor

HOW HE IS SECURED—REGULATION AND CUSTOM COMBINED.

By Z. A. LASH, K.C.

A BANKING system should afford the greatest possible measure of safety to the depositor. The relation of a bank to its depositor is that of debtor to creditor. The bank is in no sense a trustee for the depositor of the money deposited; the money in law is lent by the depositor to the bank and the bank is entitled to use it for its own benefit and to retain whatever profit may arise from such use—without liability to account therefor. There are some special incidents attached to this relationship of debtor and creditor which do not apply in the ordinary case. For instance, deposits are repayable by cheque on demand unless otherwise expressly agreed, and if a bank without valid reason refuses to cash a depositor's cheque when there are funds available, damages may be recovered for injury to the depositor's credit. The depositor has no security for repayment of his deposit other than that afforded by the ability of the bank to meet its engagements, including in this the double liability of its shareholders.

Safeguards and restrictions relating to the use which the bank may make of monies received from depositors may be established, a rigid system of Government returns published periodically may be enforced, Government inspection and fixed cash reserves may be required, the liability of the shareholders may be trebled instead of doubled, yet after all the real security of the depositor depends upon efficient management of the bank. Efficient management includes and implies proper inspection and audit and if that be withheld it is probably because the management, although capable, is positively dishonest. No one can guard against absolute dishonesty. Therefore, a system which tends to produce efficient managers skilled in the investment and loaning of money and having at hand a ready means of acquiring and keeping up accurate knowledge of local as well as of general business conditions, is more likely to afford a larger measure of safety to the depositor than a system which has not this advantage. Experience has shown that a system of banking with branches does produce efficient and skilled managers in greater numbers and with wider knowledge and experience than a system composed of separate and individual banks. It in fact creates and maintains a class of professional skilled bankers. Head office keeps in daily touch with the various branches, and frequent reports are required from the branches, not only of the affairs of their customers, but also of the business conditions in the locality. Clerks branch and moved from place to place before they become branch managers or responsible officers at head office or at branches, and even managers are transferred from place to place. In this way, in addition to learning the methods and business of his own bank, each member of the staff acquires a more thorough knowledge and grasp of general banking business and of the conditions existing all over the country than would be possible under other and more limited conditions. The Canadian banking system, therefore, possesses and will always produce efficient managers. I place efficient management first among the measures of protection to the depositor.

POWERS OF INVESTMENT.

Sections 64 to 75 inclusive, of the Act of 1890, as amended in 1900, define the general business and investment powers of a bank. They are very wide and include "such business generally as appertains to the business of banking," but there are some clearly stated and important exceptions:

It must not, except as expressly authorized by the Act, "directly or indirectly deal in the buying or selling or bartering of goods, wares and merchandise or engage or be engaged in any trade or business whatsoever, and it shall not either directly or indirectly purchase or deal in or lend money or make advances upon the security or pledge of any share of its own capital stock or of the capital stock of any bank, and it shall not either directly or indirectly lend money or make advances upon the security, mortgage or hypothecation of any land, tenements or immovable property or of any ships or other vessels or upon the security of any goods, wares and merchandise."

The principle involved in these exceptions is accepted by the bankers as sound and not to be departed from. It is this, that as the bulk of a bank's liabilities is pay-

able to depositors on demand or at short dates, the monies received from depositors shall not be tied up in loans upon, or purchases of, real estate or goods, or otherwise be so used that they cannot be readily converted so as to meet the demands of depositors. The prohibition against lending on the bank's own stock involves the same principle and the prohibition against engaging in trade, in addition to involving this principle, involves the foundation principle of all sound banking, viz., that a bank's mission is to supply the borrowing business wants of those engaged in trade and to assist, but not to compete with them in developing the resources of the country.

The prohibition against lending upon the stocks of other banks is a wise provision, as but for it a bank unscrupulously managed and having a capital of say \$1,500,000 might organize another bank with a capital of say \$500,000, and might take and pay for the whole \$500,000 of stock. The result would, of course, be that for all practical purposes the two banks would be one and the joint paid-up capitals would really be only \$1,500,000, while they technically would be two banks with joint capitals equal to \$2,000,000. Power to issue notes to the extent of \$2,000,000 would, therefore, exist, whereas this power should really be for \$1,500,000 only. Other evils might also result if this prohibition were removed.

The cases expressly mentioned in the Act which form the exceptions to the prohibitions referred to are in harmony with the principles to which I have alluded. Power to hold real estate for the proper carrying on of the business of a bank is of course a necessary incident to its existence, and power to take security on real and personal property for existing liabilities properly incurred in the course of its business is also necessary, and these powers are given. Power is also given to advance money for the building of a ship upon the security of the ship being built. This is in harmony with the encouragement of trade and commerce. The main exceptions are with reference to lending upon the security of goods, wares and merchandise.

Experience has shown that under the powers of investment and of doing business possessed by our banks they are enabled to answer well the purposes for which they exist and at the same time to make money for their shareholders. Experience has also shown that the limitations upon their powers are wise and in the interests of their depositors whose money they acquire, and that in these respects our system affords a very decided measure of safety to the depositor.

MUTUAL INTERESTS OF BANKS.

A factor bearing largely upon this question and upon which great reliance may be placed is the mutual interests of the banks in the different parts of Canada and their common interest in averting a panic or a situation which would greatly disturb business and financial circles. This common interest brings them together, when help is required, and on more than one occasion a bank in difficulties has been able, with the assistance of the other banks, to liquidate with open doors, thus avoiding the sacrifice of its assets and the inconvenience and loss to its customers which would inevitably result from the closing of its doors, and thus saving loss to its depositors and enabling it perhaps to make some return to its shareholders. In this way our system affords a real measure of security to depositors.

I will not occupy time by discussing the much debated questions of Government inspection and fixed cash reserves. Opinions as to the wisdom of these differ. They were fully debated with the Government in 1890 and the deliberate conclusion was come to, by the Government as well as by the banks, that Government inspection and fixed reserves were not suited to our conditions or to our banking system, and would be not only unnecessary and of no protection, but would be positively detrimental to the true interests of both depositor and borrower. The real protection to the depositors is what I have explained—(a) Efficient management; (b) prohibiting loans upon securities not of a liquid and convertible kind; (c) the common interest which the banks have in averting panic or a situation which would greatly disturb business and financial circles; (d) the double liability of shareholders.