

Minutes of the Nevada State Legislature
Senate Committee on Government Affairs
Date: Feb. 14, 1979
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Present: Chairman Gibson
Vice Chairman Keith Ashworth
Senator Dodge
Senator Echols
Senator Ford
Senator Kosinski
Senator Raggio

Also Present: Herb Thorndal, Bank of North Dakota
(See Attached Guest Register for
remainder of those present)

Chairman Gibson opened the tenth meeting of the Government Affairs committee at 2:00 p.m. The first order of business was the discussion of SJR-5.

SJR-5 Proposes constitutional amendments which allow legislature to establish corporate state bank.

Senator Neal, one of the sponsors, testified that although this bill was defeated last session he feels it is an important issue, and should be considered again. Senator Neal introduced Mr. Thorndal, President and Manager of the Bank of North Dakota.

Mr. Thorndal, testified to the committee that the North Dakota Bank is the only wholly state owned bank in the country. Mr. Thorndal stated that he has testified at the New York, California and Oregon legislatures and would read from his prepared testimony. (See Attachment #1) At the conclusion, Mr. Thorndal stated that he would be available for any questions.

Senator Dodge felt that we might have more incentive to look into the possibilities of a state owned bank if we had unit banking as they do in North Dakota. The Senator asked Mr. Thorndal about the procedure used by his bank on state depositors.

Mr. Thorndal replied that in 1977 they had \$244 million deposited and \$280 million deposited in 1978. He further noted that their single biggest expense in the state is the amount paid to the State Treasurer on its time money. The profits are appropriated by the State, usually to the General Fund. We are proposing, in the current legislative session, that the State only get \$14. million of the profits. It has passed the House and will be heard in the Senate this Friday. Approximately 84% of our net operating earnings have been going into a dividend to the State. We feel that our percentage is too high and the bank should be retaining more earnings to keep up the capital ratio.

Senator Kosinski asked Mr. Thorndal about the impact on the private banking industry in the state. Mr. Thorndal responded by stating that they have never done a study but the biggest impact would be in the city of Bismark. The private depositors in our bank are of a small amount because we only have the one bank, no branches. Mr. Thorndal continued that the private banks were becoming more and more dependent upon the state bank for lending power.

Senator Raggio asked Mr. Thorndal if there were any types of loans that they were unable to participate in. Mr. Thorndal stated that there were no legal restrictions on the types of loans they can participate in.

Chairman Gibson asked Mr. Thorndal who was on the managing board and Mr. Thorndal responded that the board consisted of the following; Governor, Attorney General, Commissioner of Agriculture. They are charged with the management of the bank and make the law. There is also an Advisory Board which is provided for by statute, consisting of five members appointed by the Governor with the approval of the the Industrial Commission.

Mr. Thorndal stated that at the present time those five people consist of representatives from; small manufacturing, the president of an insurance company, a farmer/rancher, retail business, and a banker. There is a bill which has passed the Senate to expand this number from five to seven members. Two of those members would have to be bankers from the private banks within the state and one from any financial institution. This would make three representatives from financial institutions and four from the general public. The only authority the advisory board has is what the Industrial Commission gives them. In North Dakota we can make loans of up to \$400,000. (in house) and anything over that amount has to go through the advisory board. Anything over one million has to be approved by the Industrial Commission.

Senator Echols stated that as a former banker he had some understanding of the banking business and had prepared some questions that might help the committee better understand the possible benefits of having a state owned bank in Nevada

- 1) It was mentioned that you have a good relationship with the private banks in the state, do you have inter-bank accounts with all of the banks in North Dakota?

Answer: Yes, we have inter-bank accounts with all the banks in the State at the present time and we have a good working relationship.

Mr. Thorndal also felt that a phase in operation for a State Bank in Nevada would be advisable. You would not want to take any more than 10% of the States funds which represent their deposits. A ten or five year phase in procedure would be reasonable. He added that 9% of their deposit base was from private sources and 65% of the deposits came from the State. The remainder comes from political subdivisions and cooperatives throughout the state.

- 2) Does the Bank of North Dakota maintain a trust department?

Answer: Not for the private sector, only for certain state trust funds. As an example; Teacher Retirement, Workmen's Compensation funds are managed by the State of North Dakota.

- 3) Does the state own the state buildings and if so do they become an asset of the state. If not, do you see any reason why the state buildings couldn't be moved into the state bank and managed by that bank.

Mr. Thorndal stated that they do not own the state banks and doesn't think it would be wise to bring them under the state banking system.

- 4) Re. \$400,000. limit on loans without approval of the advisory board mentioned in your testimony earlier, can any loan officer approve than amount or only certain individuals?

Answer: Mr. Thorndal stated that he has that that authority but since he seldom makes loans the officers in the loan department have authorization, set by Mr. Thorndal. Some of the loan officers have a limit of \$50,000 and some at \$100,000. We have an investment committee that meets every Wednesday morning, all loans that have been made are reported to that committee. If there is a loan pending, that if over that particular officers limit, the committee will vote on whether to approve the loan. If the loan is for more than \$400,000. it goes on to the Advisory board with the investment committee's approval.

- 5) Do the federal regulations interfere with the operation of the bank? What are the costs created by federal regulations.

Answer: Mr. Thorndal stated that their system is not sophisticated enough to give a cost figure on compliance with federal regulations. Since we cover the entire state the bank doesn't have to get involved in drawing up boundaries, although we do comply with all federal regulations required. Mr. Thorndal took this opportunity to state that the banking industry is concerned with compliance with federal regulations and it is a burden

Mr. Thorndal informed the committee on the procedures that his bank uses regarding unsecured loans to students. They have had a good repayment record and with a federal guarantee on this type of loan we will be able to request \$70 million bond issue, for the next three years funding. With 28,000 loans in repayment status at the present, there is less than a 2% loss ratio.

- 6) If we had a state bank in the State of Nevada, would there be any problem with making a loan package that every bank in the state could participate in ?

Answer: It could be done, our bank is working on a couple of proposals at present that we call, "up stream - down stream" financing. The banks that are heavily loaned come in to the state bank for the loan and we go back down to those banks that aren't as busy in the loan area. Its not perfected at this time but we are working on that idea.

- 7) The salary range, do the salaries of those working for the state bank compare to the private sector?

Answer: The state employees in North Dakota have a fairly low pay scale. In the bank of North Dakota a study was done comparing the bank with other banks. Our salary scale was favorable up through middle management. The higher the executive went the lower the rating went.

- 8) How does your salary, Mr. Thorndal, compare with the Governor's?

Answer: The Governor or North Dakota gets an annual salary of \$27,000. He also receives a \$13,000 unvouchered expense account. My salary is \$47,000.

- 9) Does the State of North Dakota have a usury law?

Answer: The usury law in North Dakota is a bit different than most states and has many exceptions. There is an installment loan act, retail sales act, etc. The basic usury law is 3% over the amount allowed by the banks on a 30 month C.D. under regulation Q, (6-1/2%) That makes it a 9-1/2% usury law. Exception, business loans over \$25,000. the usury is not permitted. There is no limit to loans to cooperatives and corporations. Most of the loans that the state bank has is over the usury limit.

- 10) Would it be possible for the state owned bank to be operated on a franchise basis whereby the people aren't working for the government.

Answer: This certainly could be done. Mr. Thorndal gave an example where a state owned industry became unionized.

Senator Echols concluded his questioning by informing the committee that Mr. Thorndal has been the President and Manager of the North Dakota bank since 1969 and asked Mr. Thorndal if he would be available for assistance if the state of Nevada favorably considers a state owned bank. Mr. Thorndal stated that he would be happy to help Nevada in forming its own state bank.

Dave Horton, Carson City attorney, testified on behalf of himself to the committee in favor of SJR-5. Mr. Horton passed out copies of the Congressional Record concerning the U.S. Monetary Crisis; its threat to liberty and the remedy by the Hon. John R. Rarick of Louisiana. The message was delivered in the House of Representatives on Thursday, May 11, 1972. Mr. Horton went over parts of this article for the committee and concurred with Mr. Thorndal's testimony. Mr. Horton urged the committee to appoint a study group to look into the impact a state owned bank would have on Nevada, particularly the area of municipal bonds.

Mr. Horton concluded his testimony by stating that he would like to get Mr. Thorndal's ideas on how Nevada should go about phasing in a state owned bank and what areas should be considered first.

George Vargas, legal counsel for the Nevada Banker's Association testified in opposition to SJR-5. Mr. Vargas suggested that the committee investigate why North Dakota is the only state owned bank in the United States. Mr. Vargas congratulated Mr. Thorndal and the Bank of North Dakota but felt that such a bank was not necessary in Nevada. "States as Bankers" and "State-Owned Banks: New wine for old bottles" were used in testimony. (See Att. #3 & #4) Mr. Vargas was asked to get input from the various banks on this matter and to report his findings back to the committee.

Alan McNitt, representing the Nevada Housing Commission, testified to the committee on a state owned bank and its affect on the housing division. Mr. McNitt felt that the tax exempt municipal bonds would have to pay competitive rates. The excess funds that would be invested must receive higher rates than they are getting from the bonds, anything else would lead to default of the bonds.

At this point further discussion on SJR-5 was discontinued until the committee had an opportunity to study the material presented. SJR-5 will be rescheduled for action at a later date.

SB-171 Revises designation of various accounts and funds.

John Crossley, Legislative Counsel Bureau Audit Division, testified to the committee that this bill was requested by their division to

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abolish certain funds. These funds being abolished were not being used, the accounting was being accomplished in other funds.
(See Attachment #5)

Milos Terzich, representing the American Counsel of Life Insurance testified against the passage of SB-171 in its present form with the amendments as suggested by Mr. Crossley. Mr. Terzich introduced the committee to Frank Young, General Counsel of the American Life Insurance Association. Mr. Young was in the Carson City area from Washington D.C.

Mr. Young stated that their association is concerned with the language and proposed changes to Section 57. The representatives from Nevada have had special consideration from the budget division when attending their conventions but with this new language it would be impossible for representatives from Nevada to attend without paying money out of their own pockets.

Mr. Terzich had a prepared list of amendment suggestions for the committee. (See Attachment #6) This list of suggested amendments has been reviewed by Mr. Crossley and it was felt that the changes were acceptable.

Senator Keith Ashworth moved "Amend & Do Pass" on SB-171
Seconded by Senator Ford.
Motion carried unanimously.

Amendments as per attachment #5 and #6.
Senator Dodge was asked to get the amendments prepared.

AB-176 Removes requirement to mail certain county license regulations.

Sam Mamet, representing Clark County, stated that under the current regulations they must mail out all regulation changes to all attorneys. Currently the cost is \$6,000 per year. They feel it is not necessary to mail out all license regulations to all attorneys. Mr. Mamet stated Washoe County is in favor of AB-176.

Senator Kosinski moved "Do Pass" on AB-176
Seconded by Senator Dodge
Motion carried unanimously.

SB-197 Permits certain district attorneys who reside outside their respective counties same salary as those who reside within their respective counties.

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Chairman Gibson stated that this bill came from Senator Blakemore. The new language was added to include a district attorney who does not live within the county but resides within 10 miles of the county. Currently there is a difference in salary that amounts to a \$5,000. loss to a district attorney that does not reside within the county. The remainder of the bill is unaffected.

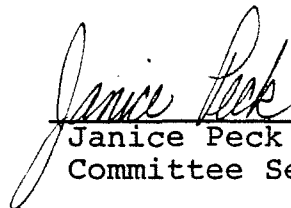
The committee felt that the bill should be amended to be effective upon passage and approval.


Senator Ford moved "Amend and Do Pass" on SB-197
Seconded by Senator Keith Ashworth
Motion carried unanimously.

Chairman Gibson discussed the scheduling of SB-72 and it was the decision of the committee to hear SB-72 on February 23, 1979 upon adjournment. The committee further decided to hear SB-120 on February 26, 1979 at 2:00 p.m.

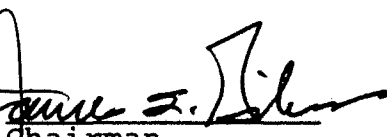
With no further business the meeting was adjourned at 5:05 p.m.

Respectfully submitted,


Janice Peck
Committee Secretaries


Lois Smith
Committee Secretaries

Approved:


Chairman
Senator James I. Gibson

Remarks

by

H. L. Thorndal, President
of the

BANK OF NORTH DAKOTA

Before

a Committee of the
Nevada State Legislature

February 14, 1979

Mr. Chairman, Members of the Committee:

Thank you for allowing me the opportunity to talk with you. My name is Herb Thorndal. I am from Bismarck, North Dakota and I am President and Manager of the Bank of North Dakota, the only wholly state-owned bank in the United States. I, and most all of my fellow North Dakotans, are proud of the Bank of North Dakota. We think we are doing things for the citizens of our state that either wouldn't get done, or at least not done as well, if it wasn't for the Bank of North Dakota's efforts.

Let me give you a little history of the Bank of North Dakota, and what we are presently doing. Bank of North Dakota was established by Act of the State Legislature in 1919. It was an outgrowth of the populist movement that started in the last century and culminated with the Non-Partisan League gaining control of North Dakota state government in the election of 1918. Even the most optimistic boosters of the idea of a state-owned bank would be surprised by the magnitude of its success today. The Bank of North Dakota was created for the purpose of "encouraging and

promoting agriculture, commerce and industry," as stated in the enabling act. Too often farmers in North Dakota, at that time, were taken advantage of by out-of-state interests, both as to marketing farm products and financing operations. Most of the banks in North Dakota, today, as they were 58 years ago, are quite small; and adequate financing often was difficult to obtain, not only for the farmer but for small manufacturing firms, economic developments, housing, student loans and other socially desirable projects. The Legislature in 1919 hoped the creation of a state-owned bank would alleviate some of the financial problems the citizens of the State were experiencing. The Bank of North Dakota is the only one of its kind in the United States. From its start, the Bank of North Dakota did not propose to enter into competition with existing banks, but to cooperate with them and assist in developing and coordinating all parts of the financial services of the State, so as best to meet the needs of the people. That policy has continued to the present day. The Bank of North Dakota feels that it is a "partner in progress" with other financial institutions in North Dakota. All one hundred seventy-three of North Dakota's banks maintain an account relationship with the Bank of North Dakota. At the time of the creation of the Bank of North Dakota, the Legislature also created the State Mill and Elevator. The State Industrial Commission was also created by the 1919 Legislature, and was charged with the operation, control and management of the Bank and the State Mill and Elevator. The Industrial Commission is composed of the Governor, who acts as Chairman, the Attorney General and the Commissioner of Agriculture. This is, I believe, as it should be. In order to be sure the Bank responds to public needs, it should

be controlled by elected officials. However, I believe the State Treasurer should be on the board.

The Bank of North Dakota officially opened business on June 20, 1919, with \$2,000,000 in capital. This \$2,000,000 in capital was provided through the sale of Bank Series Bonds, which have since been retired out of the Bank's earnings.

Since 1919, through 1978, the Bank has made net operating profits of over \$122,146,000. The Bank had total resources of over \$616,000,000 in August of 1978, when it "peaked" at its seasonal high. It had over \$581,000,000 in resources last week, as we approach our seasonal low.

The original act provided all public funds should be deposited in the Bank of North Dakota. This was changed by an initiated measure in 1921 to provide that all political subdivisions, with the exception of the State, itself, make deposits either in private institutions or in the Bank of North Dakota. At the present time, the Bank of North Dakota has approximately 10% of all public deposits, other than the State's. Because the law states that all monies of the State and State institutions must be deposited in the Bank of North Dakota, we do not have the problem of allocating funds to various financial institutions; and all political pressures are eliminated. The Bank of North Dakota pays competitive interest rates on state deposits that we set up as Time Certificates. The Bank does accept time and checking accounts from individuals and corporations, but is prohibited from making private and commercial loans, with the following exceptions: Veterans Administration (VA) and Federal Housing

Administration (FHA) guaranteed home loans and Federally Insured Student Loans (FISL), and loans to actual farmers, if secured by real estate, and not exceeding 50% of value, and to North Dakota residents if secured by stock in a North Dakota bank. The Bank of North Dakota may participate with other banks, savings and loan associations and credit unions in loans made by them. It may loan to the various departments of state government and any political subdivision within the State. All deposits in the Bank of North Dakota are guaranteed by the State of North Dakota, and we feel the State has many more assets than the Federal Deposit Insurance Corporation.

Earlier I mentioned that one of the main purposes in organizing the Bank was to promote agriculture, and in this connection, from 1919 to 1932 inclusive, the Land Department of the Bank made a total of 16,482 loans on 4,219,130 acres of land, amounting to \$38,573,000. These were financed by real estate bonds issued between 1921 and 1932. All of these bonds have long since been retired. In 1933, 1934, and 1935 approximately 8,000 tracts of land were refinanced through the Federal Land Bank and the Land Bank Commissioner. Of the remaining 8,500 tracts, about 2,000 were put on an amortized loan basis by the Land Department. This left approximately 6,500 tracts which the Bank took by foreclosure or quit claim deeds. These were sold back to the former owners, where possible, and to other interested parties. During 1941, to the present, the Bank has retained 50% of the mineral rights, which previously was 5%. All of these tracts have now been sold. We are out of the real estate business. As I stated, since 1941, the Bank has retained 50% of the mineral rights on the land they held and were selling;

which totaled approximately 750,000 mineral acres. As of July 31, 1977, the Bank has received oil revenue in the form of bonuses, rentals, and royalties in the amount of \$9,669,817.83. This is paid directly to the State Treasurer and is not part of the Bank's net operating earnings, as (earnings) reported previously. The mineral leasing function was transferred to the State School Land Department in 1977.

Because of the collapse of the agricultural economy in the 1920's and 1930's, the Bank was not the panacea for North Dakota financial problems that the State had hoped it would. However, it went a long way in alleviating the problems created by the agricultural economy collapse of the 1920's and 1930's.

In 1973, we started to get back into the farm real estate loan business. We now have over 460 farm ownership loans, amounting to over \$14 million. These 460 and some loans amount to just over 1% of all North Dakota farmers. We also service about 1400 farm real estate loans amounting to about \$45 million that belong to the State School Land funds. We expect to be even more involved in farm ownership real estate loans in the future, as we try to get and keep young people started farming.

We do have a program to finance beginning farmers. Last summer (1978) we started a program in cooperation with the Farmers Home Administration, to finance land purchases for beginning farmers. Basically, this program extends term to 40 years, may waive principal payments the first two years, and allows a reduced interest rate the first five years of the loan. This helps the "cash flow" of a beginning farmer during the "start up" years, which are the most

critical for any new business. We made 38 loans amounting to \$1.8 million the first 4 months of the program, and are processing another \$3.2 million as of today. I mention this to show that a state-owned bank can think new, innovative ideas, and put them into practice in a minimum amount of time, and without adding people to "the bureaucracy."

During the 1940's and 1950's, the Bank became the leading underwriter for political subdivision bond issues. The last few years the Bank underwrote and sold over \$12 million per year of these tax exempt issues, over \$17 million in 1978. Since the Bank pays no income tax, you might ask why do we buy tax-exempt securities? The answer is to provide an efficient and economic service to the instrumentalities of our state. Many of these issues are so small that they preclude public bidding. In the last few years, we have instituted an aggressive marketing program and our total portfolio dropped from \$30,000,000 to less than \$10,000,000. A recent Legislative Session also passed a North Dakota Bond Bank law, which is operated out of the Bank of North Dakota, allowing us to tap the national market with large issues backed up by numerous smaller tax exempt issues from around the state. Through the North Dakota Industrial Development Act, the Bank of North Dakota became the leading underwriter of Municipal Industrial Revenue Bonds. These underwriting activities are particularly helpful in a state that does not have dealer banks or home based bond dealer underwriters.

After World War II, the Bank became one of the major lenders of financing Veterans Administration (GI) and Federal Housing Administration (FHA) insured home loans. This department has since

expanded to where today it has over \$89.4 million of these mortgages from throughout the State. We were the first institution in the State to accept subsidized housing programs, such as the FHA 235 Program. The Bank of North Dakota instituted its own Interest Supplement Program to aid home buyers. We determined that a large segment of the State's population could not buy a home at today's rates. From our past experience with the FHA 235 Program, we knew that interest supplement programs work, and help some of our citizens become homeowners. Under our program, all loans are insured or guaranteed by the Federal Housing Administration or the Veterans Administration. We take 80% of a household's income, subtract an additional \$300.00 per dependent, and take 20% of the balance to determine what a household can pay for housing. We then project this to a scale to determine the rate charged, in no case more than 3% under the allowable FHA rates. This subsidy will in no case extend beyond the initial six years of the loan. We expect to reach many people in the \$14,000 to \$17,000 income range and help them to become homeowners.

North Dakota needs a housing finance agency that could issue bonds, backed up by these mortgages and this agency could be part of the Bank of North Dakota. Unfortunately, this was defeated in this session of the Legislature, but we anticipate to bring it up again if the demand for housing continues in our State. I might suggest that the State Housing Finance Agency and other similar agencies could be incorporated under one institution such as a state-owned bank.

Last December the Bank of North Dakota issued \$50 million of mortgaged backed bonds. This was the largest bond issue to have

originated in North Dakota. We received a AAA rating from both Moody's and Standard & Poors, which is rather remarkable, when you realize that our "parent" the state of North Dakota, is only rated AA. We needed this \$50 million for liquidity, so that we could continue to purchase home loans throughout our state.

In August of 1967, the Bank of North Dakota made the first Federally Insured Student Loan in the nation. Since that time, the Bank has processed 71,960 loans, amounting to over \$65,923,362.92 to students throughout the state. We are actually number two of all banks in the country (Bank of America, a \$70 billion plus bank if first) and fifth in numbers, by lender, in the number of student loans we have disbursed. We are eleventh in dollar volume. Over 60% of the Federally Insured Student Loans made in North Dakota have been processed by the Bank of North Dakota. We finance students seeking higher education throughout the world; even in Nevada. Our only requirement is that they be residents of North Dakota at the time they make the application. We generally limit vocational training to in-state schools. No schools in North Dakota act as a lender. All loans must originate with a financial institution. The reason we limit vocational schools to in-state, is we find the training costs less in North Dakota, and the danger of a student being "ripped-off" by unscrupulous proprietary schools is eliminated. In other words, we know our schools, and watch what they promise to do. We now have over 28,637 loans in repayment. The Student Loan Program is completely computerized; and we feel it is one of the most efficient lending operations in the country. It's profitable, but more important, of great benefit and service to thousands of young people, and their parents. We also buy FISL from other lenders.

We made a secondary market for FISL several years before they dreamed up Sally Mae! Our past due and claim status with the Federal Government is running less than 2%, which we feel is the best in the country. Because of the leadership of the Bank of North Dakota, our state leads the nation in making financial assistance available to students seeking education and training beyond high school.

Today we are in the process of issuing up to \$65 million in Student Loan Backed bonds. We are not going to pledge anything but student loans behind these bonds. There will be no take-out provisions, no guarantee, direct or implied on the part of the state of North Dakota, no student fees or general fund monies, and no moral obligation on the part of the state. With our very favorable repayment record, we are confident that we will get a very favorable rate. This type of financing could not be accomplished this way without the experience of a state-owned bank.

In the past, the Bank of North Dakota has made loans to various State Departments and institutions and has purchased real estate contracts from the State and its instrumentalities. At the present time, this totals only \$385,000, but in years past, this was an important part of the Bank's operation. Some examples are loans to erect a building for the Employment Security Bureau, to finance buildings for the State Fair Board, and to the State Plumbing Board. All of these were self liquidating loans, (from income). Usually, the Bank sells these loans. Since they are tax-exempt to others, we will trade for high quality, higher yielding loans. In every instance, the instrumentalities could not get a satisfactory rate until the Bank provided it. Yet the Bank is able to sell or trade

and saves money for the instrumentality.

The Bank of North Dakota starting in 1968, took a leadership position in SBA loans. Generally, the Bank will purchase the 90% guaranteed portion from the other institutions, thus providing local institutions with liquidity to take care of their other customers. We had a secondary market for SBA loans 7 years before they developed in the rest of the country. During the tight money period, in 1971 and again in 1974, the Bank accelerated its participation program with other institutions and presently has over \$118.8 million participation loans. These can be for any purpose for any time period. We anticipate this to be expanded by \$20,000,000 during 1979. This is particularly helpful to the smaller banks that have a low "legal lending limit", and this enables them to service their larger customers.

During the last legislative session a bill was introduced to get the Bank of North Dakota involved in a small way (\$3,000,000) in solar energy loans for residences. The bill failed. However, I have attended a special Regional Business and Financial Services to Develop Solar Energy Technology Transfer meeting. We expect to be involved in financing solar energy in North Dakota in the years ahead.

The Bank also serves as Trustee and Paying Agent for bond issues of the Institution of Higher Education in the state and further serves as Trustee for the North Dakota Public Retirement System and manages several State Trust Funds, whose assets are approximately \$160,000,000. In North Dakota, in 1976, we placed \$6.5 million of FHA insured home mortgages in one of our state

trust funds. Today, that market is off somewhat, but when it is right again, we may place more mortgages in these funds. All of these mortgages were purchased from, and are being serviced by, local banks and savings & loan associations. They are a good investment, yielding as much or more than out-of-state corporate bonds of the same average maturity. This investment helped the housing situation in North Dakota. It is an example of "Public money for public good!"

The Bank of North Dakota somewhat resembles a "little Fed," since we are the clearing bank for many of the institutions in North Dakota. The Bank of North Dakota has processed as high as 213,000 items (checks) a day and all of the 173 banks maintain an account with the Bank. Their combined balance averages in excess of \$20,000,000 per day.

The success of the Bank of North Dakota may be summed up by the Bank's philosophy which is, "I. To encourage and promote Agriculture, Commerce, and Industry in North Dakota. II. To provide the most efficient and economical financial services to the State, its Agencies, and Instrumentalities. III. To provide professional assistance whenever possible and wherever it will encourage and promote the well-being and advancement of North Dakota and its citizens."

The growth and soundness of the Bank of North Dakota is a tribute not only to those who conceived it and to those who have operated it, but to all North Dakotans who have benefited from the services of such an institution. The citizens of the State of North Dakota take great pride in the philosophies and soundness of the Bank.

A bank owned, operated by and for the people of a state, will not be a panacea for all of a state's economic and social problems. However, it can be of great help in alleviating many of these problems and can give leadership and financial input in isolated and special areas. I believe a state-owned bank would be a good asset for any state, and particularly to the smaller states.

I understand you will have testimony against starting a state owned bank. Let me comment on some of the usual arguments against a state owned bank:

It concentrates credit in one area - not true! The bank serves the entire state, working through other financial institutions. There is no concentration of loans in any one area.

It invests funds out of state, such as government bonds - only to the extent necessary to provide for its liquidity needs. In the past, loan demand has been increasing and we expect it to continue to increase. We presently are about 65% loaned up.

To be profitable, a state owned bank would have to compromise its purpose of advancing "socially desirable programs" - not so! We point to our record of student loans, housing loans, farm ownership loans, and municipal bond underwriting as accomplishing "socially desirable goals" and we are still more profitable than any bank in the country.

The Bank pays no taxes - We pay more into the State Treasury, as a percentage of profits, than any bank would pay in combined taxes and dividends. If you believe banks are paying large amounts into your state treasury, then I suggest you check the records.

We, the Bank of North Dakota, pay more than 7 times the amount paid by all banks and savings and loans combined in North Dakota in taxes to the state. In no way could the financial community make this up, if the Bank of North Dakota dispersed its deposits to the other institutions.

The Bank has lower expenses - True! Because of public funds having to be deposited in the bank, low occupancy expenses (we don't need the biggest, tallest, newest, most opulent building in town), little or no advertising, no give-aways (no matter how cold it has been in North Dakota, we have never given away a blanket!) and state employees wage scales. To be fair, a state-owned bank must pay competitive interest rates on time money, and the Bank of North Dakota does.

Abuse of lending authority because of political control - I believe this danger is over stated. It has never been a problem in North Dakota. Of course, we have open meeting laws. If you have a broad based board, of both public officials and representatives of the private sector, I don't see how you could have a problem.

Not able to keep capable management - If you keep partisan politics out of the bank and pay adequately, there are no problems in keeping capable management.

With the exception of the Bank of North Dakota, state-owned banks have been tried and didn't work out! - There were various reasons for the failure or discontinuance of these various experiences. Perhaps, at some time in history, the need for a state-owned bank was not necessary in some states at a certain period of time. The question being concerned in Nevada today is,

"Does Nevada need a state owned bank?"

A state owned bank is a form of "credit allocation." - True, public money for public good - what's wrong with that?

It eliminates the need for "pledging" by other banks against public deposits and weakens the market for tax exempt securities in a state. - The state-owned bank would be a market for a state's political subdivision securities. We have improved our market and I believe your proposed bank would do the same.

It can do what other banks can't do. True, that's why you want a state owned bank.

Not bound by Regulation Q - This isn't so in North Dakota. The law specifies that we can only pay rates that other banks are authorized to pay and North Dakota law refers specifically to the rates allowed by banks that are members of the Federal Reserve System. This could be included in your law, but I don't recommend that it be. From a practical experience, the proposed bank would probably only pay what other banks pay. Incidentally, in 1978 the State Treasurer had an average of almost 94% of his funds in interest bearing deposits with us and only 6% in interest free demand deposits.

Salaries of the executive officers would be higher than state officials - So what? If you are under-paying your elected officials, that's no argument about the merits of a state-owned bank.

Members of the Committee, I know a state-owned bank works in

North Dakota. I am confident it would work in Nevada. It would help your state and its citizens.

Thank you for allowing me to visit with you. I would be happy to answer questions.

"THE BANK OF NORTH DAKOTA PHILOSOPHY"

I.

TO ENCOURAGE AND PROMOTE AGRICULTURE,
COMMERCE, AND INDUSTRY
IN NORTH DAKOTA

II.

TO PROVIDE THE MOST EFFICIENT AND ECONOMICAL
FINANCIAL SERVICES TO THE STATE,
ITS AGENCIES, AND
INSTRUMENTALITIES

III.

TO PROVIDE PROFESSIONAL ASSISTANCE WHENEVER
POSSIBLE AND WHEREVER IT WILL ENCOURAGE
AND PROMOTE THE WELL BEING AND
ADVANCEMENT OF NORTH DAKOTA
AND ITS CITIZENS

H. L. Thorndal
1970

E X H I B I T 1

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HISTORY OF NET OPERATING EARNINGS (PROFITS) OF THE BANK OF NORTH DAKOTA

1919	\$ 70,276.77	1965	\$ 2,742,366.02
1920	121,883.17	1966	2,935,786.75
1921	136,259.70	1967	3,162,020.55
1922	(-273,555.84)	1968	1,913,660.64
1923	(-10,650.36)	1969	3,111,944.99
1924	25,450.35	1970	4,327,522.02
1925	114,739.00	1971	5,521,730.78
1926	(-97,472.87)	1972	6,082,929.49
1927	127,847.01	1973	8,066,384.66
1928	349,247.01	1974	9,268,770.41
1929	554,522.30	1975	8,334,877.82
1930	474,114.01	1976	9,807,755.00
1931	(-25,441.81)	1977	11,060,320.00
1932	393,348.13	1978	10,334,095.00
1933	284,007.38		
1934	301,143.18		\$ 122,146,293.98
1935	436,759.75		
1936	557,537.59		
1937	396,237.87		
1938	286,962.88		
1939	194,911.68		
1940	205,807.28		
1941	225,525.42		
1942	342,911.95		
1943	426,504.49		
1944	583,059.53		
1945	577,692.42		
1946	722,422.37		
1947	608,616.57		
1948	669,006.47		
1949	764,275.12		
1950	1,004,356.51		
1951	1,108,980.98		
1952	1,388,386.37		
1953	1,476,050.10		
1954	1,393,237.49		
1955	1,461,949.59		
1956	1,363,513.33		
1957	1,401,861.05		
1958	1,434,011.16		
1959	1,549,517.76		
1960	2,334,409.43		
1961	2,651,480.68		
1962	2,824,785.39		
1963	2,195,203.37		
1964	2,344,438.12		

Bank of North Dakota
Bismarck, North Dakota

Commercial Banking Department

LENDING PRIORITIES

The Bank of North Dakota's lending policies will be in keeping with its Philosophy: I. To encourage and promote agriculture, commerce, and industry in North Dakota. II. To provide the most efficient and economical financial services to the state, its agencies, and instrumentalities. III. To provide professional assistance whenever possible and wherever it will encourage and promote the well being and advancement of North Dakota and its citizens.

By scale:

1. Federally Insured Student Loans - Direct and Purchased.
2. Farm & Ranch Real Estate Ownership Loans to FmHA Borrowers - Direct.
3. FHA/VA Single Family Residence Loans - Direct - Purchased.
4. SBA or FmHA Guaranteed Business Loans.
5. Loans to Instrumentalities of the State of North Dakota - Direct.
6. Farm & Ranch Operating Loans, including livestock feeding.
7. Irrigation - term loans.
8. New or enlarged manufacturing - working capital, construction term.
9. Bank Stock or Bank Building loans - Direct.
10. Multi-family units, where demand warrants - FHA & participat
11. Interest Supplement Single Family FHA loans.
12. Retirement and Nursing Homes - Section 8-HUD - purchased participations.
13. Farm and Ranch Real Estate Ownership Loans - Participations.
14. Retail Establishments - construction, operating, term.
15. All others not classified above.

As a source of secondary funding for all of the financial institutions and savings and loans within North Dakota, it is our obligation to treat every credit request on its merits. We should suggest and strengthen the collateral base and documentation wherever possible. Obtain an SBA, FHA, VA or FmHA Guaranty whenever feasible and secure personal continuing general guarantees on all corporate indebtedness. Key man or term life insurance is also recommended wherever possible.

It is our obligation to encourage and promote participation and overline activity with every financial institution within the State of North Dakota. This is the entre' for increased correspondent balances, securities activity and closer ties with our respondent financial institutions; and helps us to "aid, encourage, and promote agriculture, commerce and industry in North Dakota".

General Guidelines:

1. The lead financial institution sets the rate so long as it does not exceed our "rate guide".
2. Avoid 100% participations, unless originating financial institution is already at legal lending limit.
3. Exclude speculation loans.
4. Attempt to avoid out-of-state or non-resident operator loans.
5. Accept only the guaranteed portion of SBA or FmHA loans.
6. Attempt to limit our participation on real estate loans to not more than 70% of appraisal or cost, whichever is less, and our share not more than 60% of the lead financial institution's exposure, unless lead financial institution already is at legal lending limit.

7. Encourage and promote short term (one year or less) participations to offset our long term participations.
8. On large participations or where the lead financial institution's rates are low as an accommodation to the borrower, attempt to arrange dormant compensating balances to increase our yield.
9. Attempt to place more loans on a floating rate of interest.

OPERATION PROCEDURES

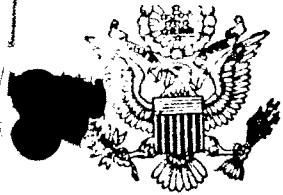
1. Have a complete worksheet and resume for the Investment Committee, Advisory Board and Industrial Commission.
2. All conversations and activity on the file with the exception of payments, shall be noted on the comment sheets and initialled by the loan officers.
3. A complete loan file including spread sheets, comment sheets, all documentation and insurance must be prepared and checked by the lending officer and double checked for completeness and full documentation by the credit department or the SBA's attorney, or our General Counsel, as the situation would require.
4. All loan files and covenants must be checked at least annually for financial statements, spreading, comments, continuations, compliance, etc.
5. Require certified CPA reports whenever possible on loans of \$250,000 or more especially if the borrower is a business.
6. Commitment letters are to detail all requirements and the copy is to be signed by the originating financial institution and the customer and returned.
7. All turned down loans are to be reviewed by two lending officers.
8. Field trips to inspect and discuss participations and overlines will be made (at least semi-annually) if staffing permits.
9. Service fees will conform to those guidelines as set forth in our "Rate Guide".

REPORTING PROCEDURES

1. Report delinquency action on a monthly basis to the Investment Committee, Advisory Board and Industrial Commission.
2. All loans, except Federally Insured Student Loans are to be reported to the Investment Committee, Advisory Board and Industrial Commission.
3. All turned down loans are to be reported to the Investment Committee.
4. A loan log will be kept of all pending loans and a monthly report on unused committed funds will be obtained by the department head and reported to the Investment Committee.
5. A monthly delinquency report on FHA-VA loans is to be made up and presented to the Investment Committee, Advisory Board and Industrial Commission.

COLLECTION PROCEDURES

1. Establish a policy of debiting and crediting the correspondent financial institution accounts for the disbursement and collection of monies on our loans, whenever possible.
2. Lending officers will be primarily responsible for collection of past due loans with the file commented regularly during the collection period. The department manager, Legal Department and President of the Bank of North Dakota will be kept regularly advised of developments and will aid in the collection procedure when their help would be beneficial.



Congressional Record

United States
of America

PROCEEDINGS AND DEBATES OF THE 92^d CONGRESS, SECOND SESSION

Vol. 118

WASHINGTON, THURSDAY, MAY 11, 1972

No. 77—Part II

U.S. MONETARY CRISIS: ITS THREAT TO LIBERTY AND THE REMEDY

HON. JOHN R. RARICK

OF LOUISIANA

IN THE HOUSE OF REPRESENTATIVES

Thursday, May 11, 1972

Mr. RARICK. Mr. Speaker, the current efforts by our Government to hold down price increases have served to focus the attention of thoughtful students on a little discussed facet of our money system. This system, because of a long process of miseducation and studied silence, is not now understood as it was prior to adoption of the Federal Reserve System more than half a century ago. It is based upon debt, has serious implications for the future of our country, and invites what may be the greatest war in history.

Every debt-dollar demands an interest tribute from our economy for every year that dollar remains in circulation. These interest costs force up the price of every commodity and service and contribute greatly to inflation.

One hundred and ten years ago, on President Lincoln's recommendation, the Congress authorized the issue of interest-free U.S. notes. Many of these notes are still in circulation and their interest-free status has saved the American economy billions of dollars.

Attempts to fight inflation in the United States by the highest interest rates here in over 100 years are bound to fail for high interest rates drive costs and prices up while holding production down. For this reason, the present administration has succeeded only in bringing about the anomalous situation of a depression in the midst of rising prices. The result has been to engorge financiers with profits at the expense of every other sector of the economy.

Moreover, so long as the manipulators of the money seek to maximize bank profits by high interest rates, prices must continue to skyrocket. Only by forcing these rates down can production be encouraged and costs reduced, which will minimize price increases.

Under the Constitution, the Congress has responsibility of issuing the Nation's money and regulating its value—article I, section 8, clause 5. In a recent brilliant analysis of our money system by T. David Horton, chairman of the executive council of the Defenders of the American Constitution, able lawyer and keen student of basic American history, he suggests a proven remedy for our current predicament that will enable the Con-

gress to resume its constitutional responsibility to regulate our Nation's money by liberating our economy from the swindle of the debt-money manipulators by the issuance of national currency in debt-free form.

Early in the present Congress I introduced legislation (H.R. 351) the main aim of which was to accomplish such liberation by authorizing our National Government to purchase the Federal Reserve System and to place it under the control of experienced administrators who recognize the basic soundness of the traditionalist money system and who can be dependent on to act in the interests of the American people and American financial needs.

In order that the indicated analysis and proposal of Mr. Horton may be available to our colleagues, I quote it as part of my remarks:

MONETARY CRISIS—ITS THREAT TO LIBERTY AND THE REMEDY

(Address of T. David Horton)

In 1797 John Adams wrote to Thomas Jefferson:

"All the perplexities, confusion and distress in America arise, not from defects of the Constitution or Confederation; not from any want of honor or virtue, as much as downright ignorance of the nature of coin, credit and circulation."

The power to issue money is the supreme prerogative of government.

The history of contemporary money policies may be traced back to what has been called "the crime of 1666" when Barbara Villiers, mistress to Charles II, helped the British East India Company gain a rake-off starting at two pence on the pound of the royal coinage. These corrupt practices were multiplied, and by 1694, William Paterson, founder of the privately owned Bank of England, would declare:

"The Bank hath benefit of the interest on all monies that it creates out of nothing."

With the crime of 1864, the National Bank Act, we find private banks gaining the power to issue money directly and a struggle commenced that has

continued to the present day. Our own national heritage, if we are allowed to know it, is full of emphatic statements upon the subject of money.

Abraham Lincoln was one of our nation's foremost statesmen on the subject of money.

The great American Monetary Historian, Alexander Del Mar, declared:

"Money is perhaps the mightiest engine to which man can lend an intelligent guidance. Unheard, unfelt, unseen, it has the power to so distribute the burdens, gratifications and opportunities of life that each individual shall enjoy that share of them to which his merits or good fortune may fairly entitle him, or, contrariwise, to dispense with them so partial a hand as to violate every principle of justice, and perpetuate a succession of . . . slaveries to the end of time."

What have we done with our money? More than a hundred years ago John C. Calhoun said that we had given the banks the government credit for nothing, only to borrow it back again at interest.

In the 1930's, Marriner Eccles, then chairman of the board of governors of the Federal Reserve System, admitted to Congressman Wright Patman that: What that privately owned central bank used to buy three billion dollars worth of government bonds was the right, as he called it, to create credit money.

Yes, banks create money — ex nihilo — out of nothing.

Congressman Usher L. Burkick confirmed this is an interview published in 1959 in which he said:

"We want to sell four billion dollars worth of bonds, and we sell it in New York to those who haven't got a dime, and they don't need any money because they simply enter credit to the government on their books! . . . And then, before such

money is paid out, they get the currency because they bundle up those bonds and bring them down here to Washington and get an equal amount of currency. Then they've got the money! But they didn't have the money before the government gave it to them."

In the meantime, of course, the government continues to pay interest on those bonds.

There is an incredulity regarding money matters that may be due in part to the fact that these gigantic legalized swindles simply boggle the imagination.

G.W.L. Day wrote in his book, "This Leads to War:"

"The mystery which has shrouded the subject of banking is every whit as deep as that which obscures the hocus-pocus of witch-doctoring; and with just the same blind respect with which the simple natives of Sumeria once gaped and goggled while their priests muttered their incantations and examined the entrails of chickens. For centuries we have listened with awe to the dictums of finance, believing that its high priesthood is possessed of knowledge superhuman and that its mysteries are sacrosanct and incomprehensible to the common run of man."

Henry Ford put it this way: "If the American people knew the corruption in our money system, there would be a revolution before morning."

What are the reasons for the disparity that we find in the manner in which we tend to accept some things, but refuse and fail to know some of the simplest of truths with regard to our money? One of the reasons may be explained this way:

We have a situation here where — if one of you deposits \$100 in a bank account and if you write checks upon that deposit twice — if you do it in my country, I have to come around and put you in jail and lock you up! You have committed a felony. Yet the very same bank in which you deposited that \$100 can write checks on that same \$100 not once, not twice, but five or 10 times, even 20 times, and can do so with impunity. This is called the fractional reserve system.

We penalize one man who writes checks on the same money twice and send him to jail.

We glorify the banker who writes checks on the same money 10 times and send him to Congress.

The difference between the banker's activity and the activity of the "paperhanger," as we'll call him, (who writes checks on the same money more than once, is that the banker charges interest for lending the same money 10 times!)

Dr. Carl F.M. Sandberg said: "From those not previously familiar with these things, have come expressions of interest and enthusiasm, but also reluctance to accept as truth the fact that our government, without getting anything whatsoever in return, gives the Federal Reserve notes to private bankers for them to loan out at interest, even back to the government itself. To them this seems so senseless as to be unbelievable."

This is one reason why we find a certain incredulity with regard to accepting some of the basic facts of life that relate to our money system. But it is not the enormity of the outrage that is most important. It is not the fact that the swindles of high finance amount to billions of dollars. It is the fact that our present debt money system does not work, that is doing us the greatest injury.

Let us consider two points about our present system.

First: That every dollar we carry around in our billfolds is a debt dollar.

Dr. Willis A. Overholser said: "Our present Federal Reserve System is a flagrant case of the government's conferring a special privilege upon bankers. The government hands to the banks its credit, at virtually no cost to the banks, for their private profit. Still worse, however, is the fact that it gives the bankers practically complete control of the amount of money that shall be in circulation. Our present money system is a debt money system. Before a dollar can circulate, a debt must be created."

The foregoing statement, with regard to the money we use for our trade today, applies alike to the dollars we carry in our pockets and also to the so-called checkbook dollars that banks create when making loans. These two sources of debt dollars make up our money.

Who profits from having all our money based on debt? To find the answer to this question, we can refer to the controllers of our commerce themselves.

Brooks Adams, the brother of Henry Adams, wrote in his book, the "Law of Civilization and Decay":

"Perhaps no financier has ever lived abler than Samuel Loyd. Certainly he understood as few men, even of later generations, have understood the mighty engine of (money). He comprehended that, with expanding trade, an inelastic currency must rise in value; he saw that, with sufficient resources at command, his class might be able to establish such a rise, almost at pleasure. . . . He perceived that, once established, a contraction of the currency might be forced to an extreme, and that when money rose beyond price, as in 1825, debtors would have to surrender their property on such terms as creditors might dictate."

Loyd was father of the Bank Act of 1844. He was no idle theoretician. He obviously knew what he was doing, and he knew that his clique could profit immensely by causing a boom-bust cycle to ravage the economy periodically.

The importance of controlling the volume of currency in circulation was pointed out by President James A. Garfield, who remarked:

"Whoever controls the volume of money in any country is absolute master of all industry and commerce."

Added to the fact that all of our money is debt money, we need to consider a second point, and that is our profit system: I remember as a small boy, puzzling myself over a problem that arose when I was reflecting upon the profits that I was making out of shoveling snow, mowing lawns, delivering newspapers, or whatever, saving up for the day when I would go to college. I figured: If I make a profit (and I'm supposed to be working to make a profit) and if everybody else is making a profit, where is the money to come from? I take my quarters and put them in a little bank — I was taking money out of circulation. My profit is what I took out of circulation. If everybody else did the same, a problem might develop.

I didn't come to any conclusions, but it was obvious to me, and it is probably obvious to any other ten-year-old, that there is a problem with regard to our money if we are to operate on a profit system.

If every business is run at a profit, then every business is creating a partial vacuum in the

money supply and this can lead, and always has led over a period of time to a cataclysm.

This is the assistance that the free enterprise system affords the controllers of our money system, when it is decided those controllers to cause a depression.

Unwittingly, so long as we tolerate a debt money system, we contribute to our own undoing.

Periodically, we get into a depression, and we're not able to distribute to our own people the very necessities of life. Willing workers are left idle, producing nothing, while products rust and food rots — for want of the money which our debt-money system deprives us.

A physician told me recently that the second most common diagnosis made today by the general practitioner is malnutrition. This is America in 1972.

At the same time, we are sending more than 100 million dollars worth of wheat to Russia, to feed their workers, who make more guns to kill our boys (and more ICBMs to threaten our cities).

Our own people are hungry, and the manipulators of our debt money system decree we send our food to enemies.

This is insane.

But we are not without remedy.

First, we must understand that our debt money system creates a vacuum in the money supply. Second, we must understand that in order to have a healthy economy with everybody making more and more goods and reflecting more and more profit we must have an expanding money supply.

So, our debt money system is exactly the wrong kind of money system that we need for a healthy economy. Rather than continually expanding the supply of money to meet the demands of ever-increasing goods and services that are being placed on the market, our debt money system decrees that that money supply shall contract because every dollar that is in circulation has a little tag on it, called interest, which commands that there must be withdrawn from circulation six cents or nine cents or 12 cents or whatever the interest rate dictates, in order for that dollar to remain in circulation another year.

The solution to this problem is not new. We can find it in the works of Abraham Lincoln that are now more than 100 years old. These quotations are from

Lincoln's speeches on money reform:

"Money is the creature of law, and the creation of the original issue of money should be maintained as an exclusive monopoly of the national government.

"The wages of men should be recognized in the structure of and in the social order as more important than the wages of money.

"No duty is more imperative on the government than the duty it owes the people to furnish them a sound and uniform currency, and of regulating the circulation of the medium of exchange so that labor will be protected from a vicious currency, and commerce will be facilitated by cheap and safe exchanges.

"The monetary needs of increasing numbers of people advancing toward higher standards of living can and should be met by the government.

"The circulation of a medium of exchange issued and backed by the government can be properly regulated . . .

"Government has the power to regulate the currency and the credit of a nation.

"Government possessing the power to create and issue currency and credit as money and enjoying the right to withdraw both currency and credit from circulation by taxation and otherwise need not and should not borrow capital at interest as the means of financing government work and public enterprise.

"The Government should create, issue and circulate all the currency and credit needed to satisfy the spending power of the government and the buying power of consumers. The privilege of creating and issuing money is not only the supreme prerogative of government, but it is the government's greatest creative opportunity.

"By the adoption of these principles, the longfelt want for a uniform medium will be satisfied.

"The taxpayers will be saved immense sums in interest, discounts and exchanges.

"The financing of all government enterprise, the maintenance of stable government and ordered progress, and the conduct of the treasury will become matters of practical administration.

"The people can and will be furnished a currency as safe as their own government.

"Money will cease to be the master and become the servant of humanity. Democracy will

rise superior to the money power."

What Lincoln was referring to was the issuance of a national currency, sometimes are referred to as Lincoln Greenbacks. I don't know how many here have seen or remember seeing what today are the remaining issue of approximately 500 million dollars that was put into circulation more than 100 years ago. They are the United States Notes which bear the red seal. Our ordinary Federal Reserve notes bear, appropriately enough, a dour black seal. These black seals are debt money. Before they may circulate, a debt must be created. A United States note with a red seal is spent into circulation and is interest free. There is no interest incurred in the issuance of it. There is no interest incurred in maintaining it in circulation.

Now, it would be interesting to note how much this original issue of Lincoln Greenbacks has saved the American taxpayer since its original issuance.

February 25 of this year was the 110th anniversary of the statute authorizing the issuance of Lincoln Greenbacks. Three hundred million dollars of them is supposed to be maintained in circulation under statute, but they have been withdrawn, or at least placed into some form that the common variety of people rarely gets to see. They have been outstanding for 110 years.

If we compute the amount necessary to redeem the principal and interest of this 300 million dollars that was saved 100 years ago by the issuance of Lincoln Greenbacks, we find that, at merely 3 per cent interest, the amount of indebtedness which would be represented, had bonds been used instead, would be 7.75 billion dollars. We are dealing, of course, with an exponential, and we find that if we paid 6 per cent, the amount that the Lincoln Greenbacks saved our taxpayers and our commerce is 182.5 billion dollars; and the amount at 7 per cent is 511.6 billion dollars.

The importance of this device that Lincoln initiated during the Civil War (which we need to copy if we are to emancipate our commerce from the thralldom of debt money) is recognized by the bankers themselves. The London Times is quoted as being the mouthpiece of high finance in John Howland Snow's book, "Government by Treason." The Times is quoted as follows, referring to the Lincoln Greenbacks:

"If that mischievous financial policy, which had its origin in the North American Republic during the late war in that country, (Civil War) should become indarated down to a fixture, then that government will furnish its own money without cost. It will pay off its debts and be without debt. It will have all the money necessary to carry on its commerce. It will become prosperous beyond precedent in the history of the civilized governments of the world. The brains and the wealth of all countries will go to North America. That government must be destroyed . . ."

This is what the bankers had to say about Lincoln Greenbacks.

If we want to try to remedy the situation where our money system, instead of expanding at a time when we need more money, contracts and thereby forces us into periodic depression, we need to adopt the measures that Lincoln initiated: Namely, the issuance of a national currency. If, coupled with this, we require the banks to lend our money not 10 or 15 times, but limit them to three times, (this would be enough) and this can be done by setting the reserve requirements at 33-1/3 per cent: If these two things are done, it will not only provide an immense source of tax-free revenue and provide our commerce with a source of money that is interest-free, but also, it will keep the banking institutions from taking away the control of the amount of money in circulation, which they now do by their fractional reserve system.

As it stands, by multiplying the number of times that the same dollar is loaned out, the banking fraternity in fact controls much more of the total purchasing power available to bid for goods than the control that is exercised by the original issuing authority. This can be stopped by doing these two things: Issuing United States notes on the one hand, and increasing reserve requirements on the other.

It has been wondered why it is we are drifting slowly, but apparently uncontrollably, toward Socialism. The answer to that perplexing question can be found in our debt money system. If we have a situation where there are two things that are drawing money out of circulation, namely the debt issuance of the currency in the first place and the profit motive in the second place, we find that it is necessary, in order to make

the economy "run at all, for this slack to be taken out.

The manner in which this is characteristically done in modern times is by means of a government deficit: Namely, the government spending more money than it takes in. The theory apparently is, that if the government operates at enough of a loss (and we've lost more than 400 billion dollars) then this will keep enough money in circulation to make up for the vacuum that the debt-money system on the one hand and the profit motive system on the other creates in the money supply. Yet, we all know it is impossible to borrow our way out of debt. We know that sooner or later in this type of operation there must be an accounting, and with that accounting we find depression.

When we come up to a period of recession or depression we find that the Socialists and the Communists are the only ones around with available remedies. The remedy that they suggest for the problem that is created by a restricted money supply, of having more productivity than you can distribute, it is the same remedy that was advocated by the fellow who decided to kill the goose that laid the golden egg. They can take care of the problem — too many golden eggs to distribute — by killing the goose. And there is no doubt it is possible to eliminate these unmarketable surpluses by restricting production. But restricting production is not the answer. It's comparable to killing the goose that laid the golden egg.

The answer is to have sufficient money. Sufficient blood supply in our economy: To have it stay viable and to have it stay prosperous. This can be done only if we get away from our debt-money system which forces us periodically into depression.

Another measure that we may consider in attempting to deal with the problems that we have in a money system that is basically diseased, is to try to establish some means of local control of local purchasing power.

The Roman Empire survived for many hundreds of years on the basis of a split control, a split authority over its money system.

The pounds, shillings, pence system in England (which was being phased out only last year) is the vestigial remainder of the original Roman monetary system. The pounds, the gold coinage, were the exclusive

prerogative of the Pontifex Maximus, or Caesar; the silver coinage was vested in certain favored municipalities and, ex senatus consulto, in certain favored princes. The bronze coinage, however, which, as the coinage of every day commerce allowed the Roman Empire to survive, was de-centralized.

And in our own country the original theory behind the Federal Reserve System was that it would provide de-centralized control. With 12 de-centralized Federal Reserve Banks, we were told, we would have an ability to adjust local needs to local demands. We know now that this was merely a pretext. It was a gigantic fraud. It never did and never was intended to do any such thing. It was a European-style central bank subject to the control of money manipulators which would keep us from having any local control of our local purchasing power.

What can we do individually in our states to offset this? One suggestion is to have other states follow the example of North Dakota. North Dakota has a bank. North Dakota is the only state in the Union that does have a bank. The Bank of North Dakota is owned and operated by that state. It allows a certain limited amount of local control of local purchasing power.

Local improvements are financed through that bank. Student loans are supported through that bank. You would not find it possible in North Dakota to get the people there to give up the Bank of North Dakota.

We have in other parts of the country, banks that are similarly named, but the Bank of Nevada, the Bank of Oregon or the Bank of California in every instance is a state chartered, privately-owned financial institution.

If we wish to copy the example of the Bank of North Dakota we will find that that bank provided its people with a source of credit that survived even the great depression of the 1930's.

Coupled to this we can institute in our local communities a certain amount of local purchasing power issued by the community itself. This can be in either one of two forms:

In one case, the merchants of a particular community can agree to honor each other's checks, payable to bearer and insured against being cleared through the bank, which would cancel them, but intended to circulate as a local currency. Those merchants in that

particular community will find that they will have authority to control a certain amount of their own local purchasing power. They will find that their own people, on whom they depend for livelihood, are less likely to trade elsewhere than they will be their own local community, as long as the currency that is there is circulating locally.

The other way to obtain local control of local purchasing power is by means of local or county vouchers circulating as currency. These vouchers can be made substantially interest-free under most state statutes. If this is done, local improvements can be made without our local governments going to the lending institutions to borrow back the very tax money that the local communities have with the commercial financial institutions.

These two means can combine to give us a certain amount of local control of local purchasing power. But the most important thing for us to concentrate on is the emancipation of our entire national currency from the thralldom of control by the money manipulators. This we can do by concentrating upon the issuance of national currency, in debt-free form.

In case too many people become alarmed of the consequences of this, it is to be pointed out that we now have a certain amount of non-interest bearing money in circulation. All of our fractional currency: That is to say, the pennies, the nickles, the dimes, the quarters and the halves, all of these are non-interest bearing in their form. They are manufactured in our mints; they are paid into circulation; circulate freely; they do not draw interest, and they provide the government a very valuable source of revenue.

In the fiscal years 1966 through 1970, inclusive, the amount of seigniorage paid into the treasury by the mints amounted to more than four billion dollars. The profit ratio on this type of currency is something on the order of six-to-one. (You end up with six times as much currency as you have cost going into making the fractional coinage).

The cost ratio in making the Federal Reserve notes is more on the order of 600 to 1. And during these same four fiscal years, in spite of the fact that more than 50 billion dollars in Federal Reserve notes was manufactured by the Bureau of Printing and Engraving and turned over to the banks — not one cent in seigniorage was paid into the treasury!

In arresting this swindle and in emancipating our commerce from a debt-money system we will find that the threat that is now posed by the Socialists and the Communists largely disappears.

Their remedies for our ills are being accepted gradually for two reasons:

One — There are no competing remedies being offered.

Two — Our debt-money system compels the government to spend more than it takes in, because this is the only way we can keep the economy going!

And this defect, this use of a debt-money system, is what is forcing us gradually, and sometimes more rapidly than many of us like to think, down the tube to Socialism.

By liberating our economy from its debt-money system, we will be safeguarding our own freedoms. Further than this, we will be protecting the world from a threat which seems ominous enough now, but if we usher in the era of prosperity that is available to us and that the bank controllers themselves admit will come to us, we will find that the threat of Socialism and Communism, even on the international scale, will largely dwindle and fade away.

Therefore, we must order our priorities. We must decide as individuals whether we are going to address ourselves to the problem of correcting a grave injustice that is perpetrated on our economy and on our government, by getting rid of a debt-money system. We must order our priorities and decide that we are going to spend our money and give of our substance and ourselves to this fight, rather than be distracted by the current, basketball game, football game or by any number of other diversions that are continually waved before us.

If we want bread and circuses, then what we're going to get is Socialism. If we want to make our principal pastime, our principal activity, the running of our own affairs and the reinstallation of Constitutional control over our currency, then we will find that the support of such organizations as the Oregon Legislative and Research Committee will reward our individual efforts, which will be responsive to a real national and local need.

Therefore, those who have elected to forego the entertainments of the hour to come here to study the question of what to do about our money system are to be commended. It is the people right here in this

auditorium upon whom the well-being of our Republic rests.

Those of us who have studied the American Revolution realize that it took a very small percentage of the American people to accomplish that. The burden rested on relatively few shoulders. The fact that we can see about us others who appear to be more interested in other things should not dissuade us. We should be prepared to give of our substance and our time to such organizations as this, that have a positive remedy that is something other than a Socialist remedy: A remedy that has been proven; a remedy that will work; and a remedy for which our posterity will thank us, if we are able to accomplish it.

STATES AS BANKERS



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PRESS OF
THE IRWIN-HODSON COMPANY
PORTLAND, OREGON

THE author desires to acknowledge the help of the various State Bankers Association Secretaries, the State Bank Supervisors, bank officers, and others connected with banking, and the several libraries consulted, for supplying historical data and documents, valuable in the preparation of this survey.

Information from booklets published by the Sound Currency Committee of the Reform Club and the National Monetary Commission; material from "History of Banking in the U. S.", Knox, "National and State Banks", Halderman, and various articles on state owned banks received through the courtesy of some of the above individuals, has been of inestimable assistance.

The first pages of this leaflet and the accompanying map are reprinted through the courtesy of the American Bankers Association, the material having first appeared in the June 1935 edition of "Banking".

T. P. CRAMER, JR.

STATES AS BANKERS

PRIOR to 1860, almost every state from the Mississippi Valley to the Atlantic Coast and from the Great Lakes to the Gulf of Mexico had, either under Colonial Government or since statehood, engaged in some form of governmental banking.

Issues of paper money, or "banks" as they were known, by the Colonies, principally for the benefit of the colonial treasuries, was started as early as 1690 by the Colony of Massachusetts. Although dates are indefinite previous to 1711, paper money had been issued by New Hampshire, Rhode Island, Connecticut, New York, and New Jersey, as well as the above mentioned Massachusetts. South Carolina followed in 1712, North Carolina in 1713, Pennsylvania in 1723, Maryland in 1734, Delaware in 1739, Virginia in 1755, and Georgia in 1760. In 1715, the Treasurer of Massachusetts issued paper money amounting to 50,000 pounds sterling. It was to be loaned out to citizens in sums not exceeding 500 pounds sterling, nor less than 50 pounds sterling to any one person, on mortgage security.

The paper money thus issued was for two purposes—to pay their own expenses, this money supposed to be redeemed by taxes, and to relieve distress of the people, and supposed to be paid by the latter back to the treasury.

In 1740, the British Parliament acted to prevent the formation in the Colonies of any companies for the purpose of issuing paper money. The Massachusetts banks previously formed therefore wound up their affairs.

After independence from England had been gained, a number of states actually engaged directly in banking on their own responsibility, and provision was included in bank charters in nearly all states prior to the Civil War, either requiring or permitting the state to subscribe for a portion of the stock.

The Federal Government subscribed for two million dollars or 1/5th of the capital in the First Bank of the United States, and for 1/5th of the 35 million dollars capital of the Second Bank. According to Prof. G. S. Callender, all the older

states with the exception of New Jersey and two or three 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. About this time, the northern states ceased to make further investments of this character, though in some cases ownership continued much longer. For instance, Pennsylvania did not sell the state owned bank stock until 1833. Southern, Southwestern, and Western states, which established governmental banks, held a much larger amount for a much longer time. In 1839, Georgia owned between three and four million dollars worth; South Carolina owned all the stock of the Bank of the State of South Carolina, amounting to \$1,156,318. In Virginia, a large part of the internal improvement fund, amounting to \$1,185,000, was made up of bank stock.

In the Western states, beginning about 1820, funds invested in bank stock by the state were not derived from revenue, but from sale of state bonds. Louisiana, in 1824, was the first state to do this on a sizeable scale, and in the next sixteen years Western, Southern, and Southwestern states, including the Territory of Florida, issued over 65 million dollars in bonds to provide banking capital to banking corporations. These investments were not made with the desire to encourage the growth of banking. Banks needed no such encouragements. They were, however, regarded as profitable enterprises, and the investment of capital therein as a distinct privilege. The issuing of circulating notes and the loaning of the money created thereby was the basis of bank profits.

Almost as universal as was this practice were the unfavorable results gained therefrom. In his book, "History of Banking in the U. S.", John J. Knox, former Comptroller of the Currency, says, "The creation of wealth by means of bank notes was the great heresy of the period between the years 1811 and 1861 * * *"

Being human, we are prone to forget former experiences and resort to unsuccessful theories and practices of the past because of the "new era" in which we live. This is well demonstrated in attempts made in the 1935 legislative sessions of the various states.

In nine states stretching all the way across the country, bills were introduced to put the states back in the banking business.

These states were Massachusetts, Wisconsin, Minnesota, Nebraska, Iowa, Montana, Washington, California, and Oregon. In none of them, as this is written, had the attempts been successful, and in none of the legislatures that had adjourned up to June 1 did the proposal receive much support.

In these nine states, the proposals varied widely. Central reserve banks, state savings banks, banks for limited custody of public funds, banks for compulsory custody of all public funds and for optional custody of private funds, with loans on real estate and commodities, were included in the various bills introduced. In at least two states, no capital whatever was provided, and in two or more all deposits were to be guaranteed by the state with no guaranty fund or method of setting one up provided.

With conservative New England, progressive Wisconsin, and seven other states of varying degrees of conservatism and progressivism considering these proposals, it behooves bankers, manufacturers, business and professional men, farmers, in fact all who pay taxes, to look squarely in the eye the results of past endeavors and ask themselves, "does it pay?"

It is no accident that prior to experience with state owned banks, many of our states contained provisions in their constitutions, which were reversed after having experience, of which the provisions in the Illinois constitution are typical. From the constitution of 1818: "There shall be no other banks or monied institutions in the state than those already provided by law, *except a state bank and its branches*, which may be established and regulated by the General Assembly of the state as they may think proper."

But after thirty years' experience, note the provision in the Illinois constitution of 1848 as follows: "*No State Bank shall hereafter be created*, nor shall the state own or be liable for any stock in any corporation or joint stock association for banking purposes, now created, or to be hereafter created."

Among other states, Indiana, Missouri, Alabama, Arkansas, and Mississippi, all of which tried state banking with varying degrees of success, show similar constitutional provisions before and after their experience.

The period 1800-1850 was one of rapid expansion and that same period saw the development and failure of most of the systems of state banks. In spite of popular demand, some of the

ablest citizens and legislators foresaw and foretold the effect of a currency system founded on promises alone. It must be remembered that the First and Second Banks of the United States were in existence during a large part of this period. With specie in limited quantity available and the Bank of the United States only partially successful in supplying the demands for a circulating medium in the rapidly developing country, it was natural, especially when it became evident that the opposition of President Jackson would prevent recharter of the Second Bank of the United States, that the demands of the citizens for a circulating medium should turn to their state governments. Banks were then "banks of issue", not "banks of deposit".

The reasoning of the advocates of state owned banks is well set out in a series of editorials appearing in the Cincinnati "Republican" in 1833, extracts from which read: "The West will be compelled to rely upon its own resources, upon its own schemes of finance, and the more speedily those resources and schemes are developed and matured, the better prepared it will be to meet the approaching crisis. Many of our sister states in the Valley of the Mississippi have with laudable foresight prepared themselves for the expected emergency. The States of Louisiana, Mississippi, Alabama, and Tennessee have already provided themselves with state banks formed on the most liberal and salutary principles and Kentucky and Indiana are about to follow their example. * * * It hence becomes imperiously the duty of the people of the West to themselves, to inquire by what means a sufficiency of capital adequate to all their wants and applicable to all the exigencies of their trade and internal improvements can be created and secured amongst themselves; and in order to derive all the advantages incident to its use to have that capital placed on a basis of permanency—not subject to the contingencies and fluctuations of Eastern money markets, to the caprices of lenders, or to the grasp of the selfish and avaricious."

"Instead of paying to foreign or Eastern capitalists 9% in dividends, let the money necessary to the business and prosperity of Ohio be obtained directly from the East or from Europe at 4%. * * * Let this difference, being the profits arising from dividends on the stock, be applied to the gradual and certain payment of capital thus borrowed. * * * In a state bank, every citizen will be interested in the circulation of the notes of the

bank—for the profits arising from the circulation will belong to *all the people*. Though no direct dividends will be made to the people, the profits thereof indirectly diffused will be equally secured, equally realized in the general reduction of taxation."

Contrast with this argument, statements made on the floor of the Illinois Assembly, when in 1819, the charter of a State Bank was under discussion. Those who opposed the scheme stated that "all banking institutions, even when founded upon a specie capital, are, in our opinion, dangerous to civil liberty—the public and private morals of our citizens." The corruption of the moral fibre of the citizenry would come from putting "a means into their hands whereby they will have a quick and easy access to every luxury and vice". The prediction was made that such a bank would not last ten years and the idea that it could maintain bank and state credit was called "an idle calculation, a visionary phantom, the acme of legislative folly, calculated to deceive the credulous, honest, and industrious part of the community."

It was further predicted that the bank would become a "hobby horse by which some political demagogue would ride into power", and stated that "No part of our citizens, either commercial, manufacturing or agricultural, require any such currency." Practically without exception, these predictions came true.

There were three general types of these state banking institutions; first, banks in which the state contributed a large share of the capital and in which the state had a large share of the management through directors appointed by it, the balance of both capital and management coming from private sources. The following banks were of this type: The First and Second Banks of Kentucky, 1806 and 1834; The Farmers' Bank of Delaware, 1807 (still in existence); The State Bank of North Carolina, 1811; and the Bank of the State of North Carolina, 1833; The Bank of the State of Tennessee, 1811; the Planters' Bank, 1832; and the Union Bank, 1833 (Tennessee); The State Bank of Indiana, 1814; and the State Bank, also Indiana, 1834; The Bank of the State of Georgia, 1815; and the Bank of Darien, Georgia, 1818; The Bank of the State of Mississippi, 1818; and the Planters' Bank of Mississippi, 1830; The Bank of Louisiana, 1824; the State Bank of Illinois, 1835; the Bank of Illinois at Shawneetown, 1838; and the Bank of the State of Missouri, 1837.

In the second group were the so-called real estate banks. The actual capital of these institutions was secured by the sale of bonds issued by the state and to the bank for that specific purpose. The state was not necessarily a stockholder, but usually received a portion or all the profits as compensation for the lending of its credit to the institution. Inasmuch as the working capital was furnished by the state, the stockholders did not put up cash, but secured their stock subscriptions by giving real estate mortgages. It was usual in these banks that the stockholders were the principal borrowers. Typical banks of this type were The Union Bank of Florida, 1833; the Union Bank of Louisiana, 1836; the Mississippi Union Bank, 1838; the State Bank of Arkansas, and the Arkansas Real Estate Bank, both 1836.

Still another group of banks were those in which the state furnished the entire capital and which were naturally under the direct control of the state. Under this heading might be put the State Bank of Vermont, 1806; the Bank of the Commonwealth of Kentucky, 1820; The Bank of the State of South Carolina, 1812; The State Bank of Illinois, 1821; the State Bank of Tennessee, 1820; The Bank of Tennessee, 1838; The Bank of the State of Alabama, 1823; The Central Bank of Georgia, 1829; the so-called Loan Association of Missouri, 1821; The State Bank of Iowa, 1858; and the Bank of North Dakota, 1919.

One general statement may be made with respect to most of these banks, and that is that practically all of them operated branches. Some of these were in the nature of independent banks; others were true branches; while still others issued their own notes but were directed by the parent bank as to general policy. Still other states engaged in the banking business in one way or another, and owned bank stock, but it is difficult to place their banks in any of the three general classifications.

The reasons why the states, and formerly the Colonies originally engaged in banking may be summarized as follows: First and undoubtedly foremost, at least, in the Colonial days, was the desire to furnish a circulating medium. Second, came the desire that the government share in the anticipated large profits, and third, that the government should have some voice in bank management and thus check policies which might be contrary to public interest. Fourth, private, local capital was hard to obtain and in some frontier states almost non-existent, and fifth, govern-

ment stock ownership would make the governing body a preferred customer when it desired to borrow.

To what extent were these desires realized?

The Colonial "banks" or issues of paper money provided a circulating medium of varying degrees of success. To the extent the paper was generally accepted without discount, the schemes were successful, but this acceptance, except in a few isolated cases, constantly decreased in proportion to the distance away from home the bills were presented. New England paper was at a heavy discount in the South, and vice versa, even when generally accepted at home, which was by no means always the case. The later state owned or state sponsored corporate banking institutions that were formed primarily for the issuance of currency were but little more successful. Notable exceptions to this general rule may be found in the Second State Bank of Indiana, the State Bank of Iowa, the State Bank of Missouri, The Farmers Bank of Delaware, and a very few others.

The second desire, to share in profits, was satisfied to the extent the banks successfully handled their paper issues. If the paper was not accepted, the bank folded up, and the profits did not exist. Anticipated profits in some states were turned into deficits of millions, even in those days when the word "Million" was not so glibly used. Notable examples of heavy losses may be found in the Bank of the State of Alabama, the Bank of the State of Arkansas, the Arkansas Real Estate Bank, the Union Bank of Mississippi, and others. More recently, the Bank of North Dakota has cost the taxpayers of that state some millions of dollars, though under slightly different circumstances.

The third reason for government capital, namely, supervision of policies, has been carried out through the years, though until recently without stock ownership. Supervision of banking policies under the old state owned banks, was more political than anything else. By way of example, the directors of the State Bank of Illinois, and directors of a number of other state banks, were elected by the legislature. Management gradually fell into the hands of "politicians who combined ignorance and viciousness in (their) management." The management by the state elected directorate prompted the Governor of Illinois in 1826 in his message to the legislature to remark that the directors "either

were then or expected to be candidates for office. Lending to everybody and refusing none was the surest road to popularity." Since these state banks passed out of existence, up to two years ago states and Federal Government alike had carried on supervision, gradually becoming more strict, without stock ownership. The Reconstruction Finance Corporation now owns stock in some thousands of banks, but supervision thereof is still largely left in the hands of previously constituted authorities.

The non-existence of local capital was largely overcome, temporarily at least, by these banks. As long as they operated and to the extent they brought in capital for organization by sale of state bonds in eastern and foreign markets, the capital stringency was relieved. However, repudiation of bonds soon put a serious crimp in European sales of state bonds. Among the states which repudiated were Florida, approximately 9 million; Arkansas, 500 thousand; Mississippi, 7 million, and a few others. Of some millions in state bonds sold for such purposes, a substantial proportion thereof were sold in England, the repudiation of which, along with bonds issued for other purposes also, including some by northern states, caused the following parody on Yankee Doodle to be current in London:

"Yankee Doodle borrows cash
Yankee Doodle spends it
And then he snaps his fingers at
The jolly flat who lends it.
Ask him when he means to pay
He shows no hesitation,
But says he'll take the shortest way
And that's Repudiation.

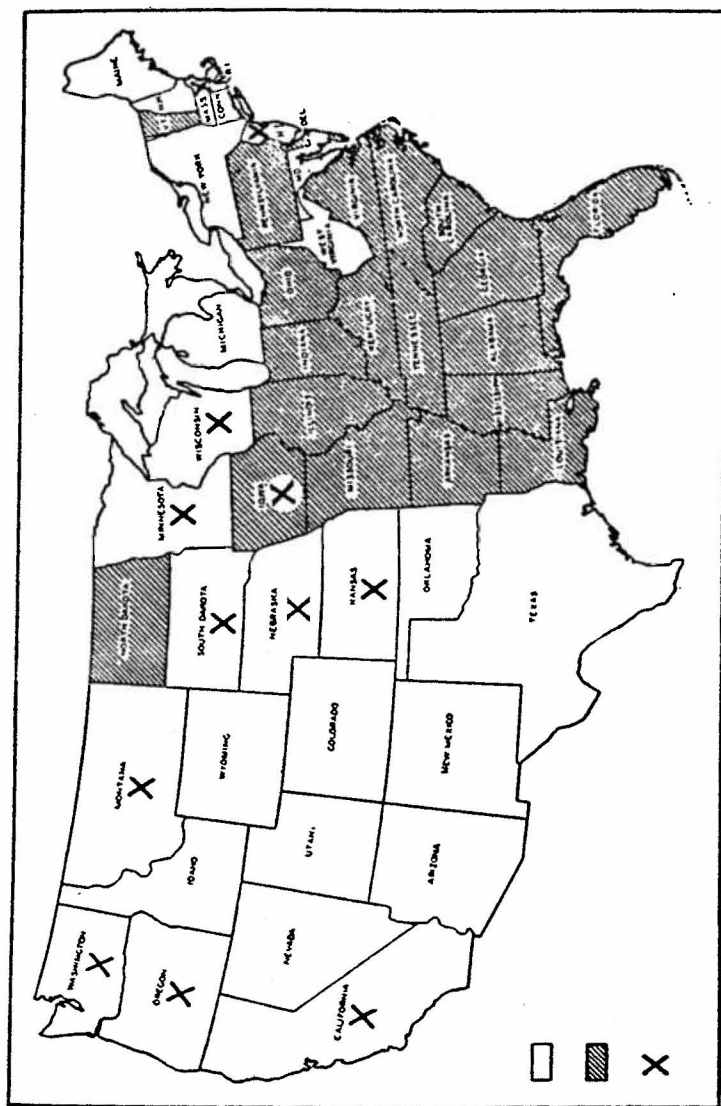
Great and free Amerikee
With all the world is vying,
That she the 'land of promise' is
There's surely no denying.
But be it known henceforth to all
Who hold their I.O.U.'s sirs,
A Yankee Doodle promise is
A Yankee Doodle Do, sirs."

To what extent the states were able to realize on the fifth reason, preference in borrowings, cannot be definitely stated. Sufficient evidence remains that the states borrowed generously. Borrowings for current operating expenses in anticipation of tax revenues were common. State officers, court judges, and other officials were compelled to accept their wages in depreciated currency, worth as low as 50% of its face, but which had been received at par in payment of taxes. Missouri, Illinois, Louisiana, and other states borrowed substantially from the banks they had created and owned either in whole or in part.

Which one of these three types of state owned or operated banks was the most successful will always be a matter of debate. In some states, such as Kentucky, Illinois, Tennessee, Florida, Mississippi, and Alabama, the purely state management resulted disastrously; while similar banks in Ohio and Indiana were well managed and solvent institutions. In Kentucky, Illinois, Indiana, and Tennessee, more than one bank was established which was managed by the state, the success of these institutions varying within the same state. The banking system of Louisiana succeeded very well under laws almost identical with those systems in Alabama, Mississippi, and Florida, which Knox calls "ridiculous failures".

Two things stand out, however; one, that with the single exception of Iowa, no state that experienced state operated banks in the past is represented in those advocating reestablishing the same in the legislatures this past winter. None of the eight other states have had state owned or operated institutions, possibly thereby explaining some of the enthusiasm voiced by the present sponsors thereof. The single exception, Iowa, had probably the most successful experience in state banking of any of the states. The other outstanding feature is that the state banks, subject to control by political authority either direct or indirect, were failures to a far greater extent than the state sponsored banks whose policies and boards of directors were not dominated by these elevated to authority by popular vote. The latter were successes to almost the same extent the former were failures.

In his book, "History of Modern Banks of Issue", Charles A. Conant makes this comment, "The creation and collapse of banks owned and managed by the states is one of the most dismal



White States—Have never tried State Banking.
 Shaded States—Have tried State Banking.
 States marked with X—At present some advocacy of State Banking.

chapters in American banking history." Warren M. Persons in his recent book, "Government Experimentation in Business", says, "Not understanding banking, but lured by the large profits which, it was claimed, were accruing to the private bankers of the period, the legislatures decided that the states should go into the banking business. The lure, this time, was the mirage of an El Dorado and taxless state. Again the enthusiasts ignored the obstacles to the success of their project, the incompetency of political management of business, and the pressure of special interests." According to A. Barton Hepburn, "The banks of states proved in most instances costly experiments. Political influence entered into the management and control in many commonwealths to the great detriment of their business interests and where states had issued bonds to capitalize such banks, the people had them to pay by means of taxation."

The proof of these comments may be found in the following state by state summary of the results of these past experiments.

ALABAMA

In 1816, the territorial government was authorized to subscribe one-tenth, one-fifth, and two-fifths respectively, in the stock of the first three banks. Apparently, however, all the stock was subscribed without state aid. When the state constitution was adopted in 1819, a state bank was provided for conditioned on the state holding two-fifths of the capital stock.

The Bank of the State of Alabama was incorporated by the first General Assembly with \$2,000,000 capital, of which \$600,000 was reserved for the state and the bank located at Cahawba. It was governed by the unlucky number of thirteen directors and passed out of existence in less than three years. In 1823, another

Bank of the State of Alabama was established, according to the preamble "to secure an undepreciating circulation." The capital all came from the state. Again thirteen directors were provided, all to be elected annually by the General Assembly. Three branches were established, but their charters were repealed in 1843. The charter of the Bank of the State expired in 1845, and was not renewed. It had received almost \$16,000,000 from the State, seven and one-half million having been poured in during the 1837 panic to avert closing. The state contributed capital of \$14,000,000, and school funds of \$1,600,000 were lost when the bank went into liquidation. However, for about ten years, the bank had paid the expenses of state government. All depositors were paid off in full, largely through the efforts of Hon. Francis S. Lyon, who used a substantial portion of his personal fortune in so doing. Politics had entered into the management and because of privileges granted directors, liberal favors were promised members of the Assembly in return for their votes. Legislators were therefore tempted to elect the highest bidders as directors. The state had a debt outside of the amount realized from liquidation of nearly \$8,000,000, all of which was paid by taxation. Two-fifths of the stock of the Planters and Merchants Bank of Mobile, chartered in 1836, and which failed in 1842, was also held by the state. The Constitution of 1867 provided "The state shall not be a stockholder in any bank, nor shall the credit of the state ever be loaned to any banking company or association or corporation." There is no substantial sentiment today for a return to state banking.

ARIZONA

The State of Arizona has never engaged directly or indirectly in the banking business. Although a law was passed by the people in 1914, authorizing the State Board of Control, among other things, to "establish, operate, conduct and maintain a state banking system for the use and benefit of the people of the state," the Supreme Court of the state held the law unconstitutional in 1928 on the grounds that the act attempted to delegate legislative power to the Board of Control.

ARKANSAS

Arkansas came into the Union just as the panic of 1837 was starting. The first act of the first legislature was to establish the Real Estate Bank of Arkansas. The second act of the legislature was one to incorporate the Bank of the State of Arkansas. The Real Estate Bank had a capital of \$2,000,000, and the Bank of the State \$1,000,000, all raised on the basis of state bonds, on which interest and sinking fund were to be paid by the banks, but on which the state was surety.

Branches were established by both banks. Funds of the Real Estate Bank were lent to farmers on long term mortgages, the interest received thereon supposed to pay expenses of the bank, plus bond interest and sinking fund. In 1841, the bank failed to pay bond interest, and it was put in liquidation in 1842. Subscribers to stock in the bank paid in nothing, but secured their subscriptions with real estate mortgages. Working capital came from the sale of the state bonds.

The Bank of the State was no more successful than the Real Estate Bank. It also failed to pay bond interest in 1841, but was not put in liquidation till 1843. Assets of these banks were insufficient to pay the liabilities and the taxpayers paid a bond issue of some \$5,000,000, this covering principal and interest on defaulted issues. Some \$500,000 of the original bond issue to the Bank of the State were hypothecated and rehypothecated until they lodged in England in the hands of the Holfords. These were eventually repudiated.

There is no sentiment today for a return of state owned banks, and the Constitution prohibits stock ownership by the state in any except corporations for charitable, educational or penal purposes.

CALIFORNIA

The state has never engaged in the banking business; in fact, the matter of a state-owned and operated bank has never been before the electorate, and there is little sentiment for such a proposition at this time, although an unsuccessful attempt was made by initiative petition to put a measure providing for a state bank on the ballot in November, 1934. The California Bank Act

of 1909 states that only a corporation organized for the purpose of banking and meeting the qualifications of the Act can engage in the banking business in that state. This would appear to eliminate the possibility of any state owned or operated institution. Nevertheless, in the 1935 Legislature, a proposal was submitted whereby the Governor, Lieutenant Governor, State Treasurer, Secretary of State, and the Attorney General were to be designated as the State Bank Board, with power to establish state owned banks to do a general banking business, one for each 25,000 population, throughout the state, with minimum capital of \$25,000.

No funds were appropriated and no subscription provided for on the part of the state toward capital, although it was provided in the act that the legislature should enact "whatever legislation is necessary for the establishment and operation of state-owned banks."

Of particular interest were: a proposal for a pension fund for officers and employees; a requirement that the executive officers have not less than ten years active banking experience; and a prohibition against purchase of or loans against corporate stocks of any kind except stock of the state-owned bank.

COLORADO

The electorate of the state has never had the proposition of a state owned bank before them, nor is there any sentiment for one.

CONNECTICUT

As in other of the thirteen Colonies, paper money was issued by the Colonial Government of Connecticut. About 8000 pounds sterling was put out in 1709. The first incorporated bank was the Hartford Bank, organized in 1792, with capital of \$100,000, and a provision that no one but the state could hold more than 30 shares, but that the state might take 40 additional shares and appoint two directors. The state has long since been out of the banking business. There is no demand from the residents of Connecticut for reentry, but there is neither constitutional nor statutory prohibition against it.

DELAWARE

The Farmers Bank of Delaware, chartered in 1807, with the state owning one-fifth of the \$500,000 capital is still in existence. State ownership of stock has continued throughout the years. Branches of the head office at Dover were established at Newcastle, Georgetown, and Wilmington. The latter two are still operated. The state appoints three directors of the head office and three for each branch, therefore, nine of the twenty-seven are state appointees, but the management is independent, and policies neither dictated nor dominated by the state. All state, county, and court funds must be deposited in the Farmers Bank, but there are no other restrictions beyond those that apply to other banks. Twenty-seven per cent of the outstanding capital is owned by the state. Delaware has also owned stock in the Union National Bank and National Bank of Delaware, both of Wilmington, and the National Bank of Smyrna.

DISTRICT OF COLUMBIA

Because of the place held by the Federal Government in directing the political and governmental activities of the District of Columbia, no bank stock has ever been held by the District.

FLORIDA

Between 1829 and 1837, several banks were incorporated by the Territorial legislature, and \$9,000,000 in bonds authorized for their aid. These included the Bank of Florida, the Central Bank, which succeeded it, the Bank of West Florida, Merchants and Planters Bank, the Commercial Bank, the Bank of Pensacola, and the Union Bank, as well as the Southern Life Insurance and Trust Company. All apparently had received some aid from the territory through stock subscriptions, bond issues or both. For instance, two hundred and fifty shares in the Bank of Florida had been reserved for the Territory. Most of these banks were organized in the same manner as were other banks in the South, the Territory advancing its credit to the banks by guaranteeing bonds on which the bank assumed payment of principal and interest. Proceeds were then available to the bank, stockholders having generally paid in nothing but secured their subscriptions by giving real estate mortgages.

Florida was admitted to the Union in 1845, and by the time the state was two years old, all banks except the Union Bank and Southern Life Insurance and Trust Co. had passed out of the picture and the State thereafter at no time recognized the corporate existence of these two territorially created institutions. The history of the Union Bank is typical. It was chartered in 1833, with a capital of \$1,000,000, which could be increased to \$3,000,000. The stockholders were not required to pay for any of their stock subscription in money, but only to secure it as previously outlined. Seven directors were to be annually elected by the stockholders and five appointed by the Governor. Interest and principal on the \$3,000,000 of bonds pledged by the state was to be paid by the bank, but in the event of failure to pay, the government was liable. After all bonds were paid for, one-half the profits were to go to the territory. By the sale of bonds, the bank obtained \$1,000,000 capital, and in 1838, an additional \$2,000,000 in bonds was delivered to the bank. Before all the bonds were sold, the question was raised as to whether the territory could legally issue them without the consent of Congress. Inasmuch as Congressional disapproval had not been voiced, the bonds were held by the courts to be legal. The electorate, nevertheless, repudiated the debt. When Florida became a state, the existence of these banking institutions was denied by the state government, and in 1851, there were no banking institutions except those chartered outside the state, and with agencies in Florida. In 1851, an elaborate charter was granted the State Bank of Florida, but was apparently never established, and in 1855 the Bank of the State of Florida was granted another elaborate charter. As in some other Southern states, the Civil War wiped out this institution. Since that time, the proposition has not been before the electorate.

GEORGIA

Prior to and during the Revolutionary War, Georgia, like all the Colonies, issued paper money and designated it as legal tender. The first issue was apparently in 1760, and other issues as late as 1786. The Federal Constitution prohibited the issue of bills of credit, but shortly after the turn of the century, the state embarked in banking.

The Planters' Bank was chartered in Savannah in 1807, but the organization was not then completed. The Bank of Augusta was chartered in 1810, with \$300,000 capital, and increased until it amounted to \$1,200,000, of which the state held \$200,000. The sponsors of the Bank of Savannah obtained a new charter for the Planters' Bank in 1810, with an authorized capital of \$1,000,000, of which 10% was reserved for the state. In 1815, the Bank of the State of Georgia was incorporated at Savannah, with a million and a half capital, of which the state reserved \$600,000, and in 1816, the Bank of Darien, with a capital of \$1,000,000 was chartered, with the state subscribing for \$500,000. Out of its holdings in these four banks, the state in 1828 developed the idea for a central bank, without any capital except the shares that it held in the four previously chartered institutions. This was known as the Central Bank, and located at the state capital, Milledgeville. It was in active operation until 1842, when it went into liquidation, but did not wind up its affairs until 1856. Although the profits from the Central Bank enabled the state to conduct its affairs without taxation for some time, and noteholders and individual creditors were paid in full, the state lost heavily by loss of deposits, as well as stock, and eventually had to issue bonds to redeem its outstanding bill. In the Bank of the State of Georgia, the state increased its holdings in 1848 by \$150,000. This institution continued to be prosperous for some years, but the events of the Civil War swept it away. Stock in some of these banks, valued as worthless, was carried on the books of the state in 1889, when the legislature authorized the State Treasurer to write it off and file the certificates.

From time to time suggestions have been made that the state organize a state controlled central or reserve bank, but the suggestion has met with little enthusiasm, and even less consideration.

IDAHO

The state has neither during territorial days nor since statehood engaged in the banking business. The electorate has never had the question before them, and there is apparently no substantial sentiment for any such plan. The state constitution forbids the state from loaning its credit, which indirectly would prohibit state banking, but there is no statutory prohibition.

EXHIBIT 3 101

ILLINOIS

Sentiment in Illinois in the two or three decades following the turn of the last century was typical of the rapidly developing mid-western states. It was felt that the only thing needed for development was capital, and that this could be best supplied by banks of issue. The first bank in Illinois was that started at Shawneetown in 1813 with \$300,000 capital, one-third of which might be subscribed by the territory. The Bank of Edwardsville was incorporated in 1818, also with \$300,000 capital and one-third reserved for the territory. After several years' successful operation, the Bank of Edwardsville closed with deposit loss, as well as loss to stockholders. The Bank of Shawneetown closed in 1823, but paid both public and private debts, remained inactive for several years, and reopened in 1835.

The state constitution of 1818 prohibited the establishment of any new bank except a state bank and its branches. In March, 1819, the State Bank of Illinois was chartered, with \$4,000,000 capital, half of which was reserved for the state. It never engaged in business. In 1821 the legislature passed an act establishing the State Bank of Illinois, with \$500,000 capital, based entirely on credit of the state. Five branches were authorized, with the president, six directors of the head office, and five for each branch elected by the legislature. This bank went into liquidation, and its affairs were practically closed by 1831. The state lost about \$400,000.

In 1835, the State Bank of Illinois of Springfield was established with \$1,500,000 capital, \$100,000 of which was reserved to the state, and with the privilege of increasing the capital to \$2,500,000. It opened with five branches in other towns and later on four more were established. The same day this bank was chartered, the Bank of Shawneetown was rechartered. The original one-third of the capital had not been taken by the territory. This was now taken by the state, along with an additional \$1,000,000, and \$400,000 more subscribed privately. In 1837, an additional \$2,000,000 was provided by the state for the State Bank of Illinois. The panic of 1837 caused suspension of the State Bank. It thereafter resumed temporarily, suspended again late in 1839, resumed briefly in 1840, and then suspended permanently. It was definitely placed in liquidation in 1843. A

legislative investigation of the bank during this period showed that politics had influenced management, and that the bank had served speculators instead of the business and public interests of the state. The failure of the state bank, with \$3,000,000 outstanding circulation, took with it a few months later, the Bank of Shawneetown, with circulation of \$1,700,000. The Constitution of 1848 prohibited the creation of a state bank and there is no sentiment for one today.

INDIANA

When Indiana became a state in 1816, two banks that had been chartered by the territorial government in 1814 were in operation, the Bank of Vincennes and the Farmers and Mechanics Bank of Madison. The charter of the latter provided that the territory might subscribe for stock at any time. The 1816 Constitution carried a proviso continuing the two banks, and a further proviso that the state might at any time designate one of them as the State Bank. In 1817, the Bank of Vincennes was so named, and a branch established at Madison by taking over the bank already in existence. The capital of the Bank of Vincennes was increased by \$1,000,000, and 3752 shares reserved for the state, which was neither subscribed nor paid for. Three other branches were established, but in 1821, when the bank was placed in liquidation, although the branch at Madison paid all depositors and holders of its bills and continued to operate independently, neither depositors nor billholders in the parent bank and its other branches received anything.

The Madison bank apparently closed later, for when the State Bank of Indiana was chartered in 1834, there were no other banks of any character operating in the state. This bank had capital of \$1,600,000 divided equally among ten branches, and of which the state owned half. Three other branches were organized later. The state elected the President and four of the seven directors of the parent bank, and half the directors of the branches. The latter did all the banking, the parent bank being supervisory only. Great care was exercised in the banking business. The bank had a complete monopoly, and it is claimed that in 25 years of operation and loaning millions of dollars, losses did not equal \$50,000. Over 3½ million dollars profits

accrued to the state on the \$1,800,000 capital, and the bank successfully survived the panic of 1837. Before it became time for the charter to expire, a provision was put in the state Constitution by the people in 1851, prohibiting the state owning stock in any bank. Before the charter of the State Bank of Indiana expired in 1857, however, the legislature chartered the Bank of the State of Indiana over the Governor's veto in 1855, in which the state owned no stock. Twenty branches were authorized. This bank was organized by politicians for speculative purposes, but finally negotiations were opened for purchase of the branches of the old bank. Hugh McCulloch, first Comptroller of the Currency, was president of the branch at Ft. Wayne, and became president of the new parent bank. When the branches of the old bank were purchased, most of the officials thereof came to the new bank, and with President McCulloch, made a success thereof. The state, however, no longer had the right to name any of the directors or the president. In the panic of 1859, the Bank of the State of Indiana and Bank of Kentucky were the only two banks in the West that did not suspend specie payment. When the national bank law was passed, all but three branches became national banks. One of the three liquidated and the other two changed into private banks.

There is little or no sentiment in Indiana today for a state owned bank, and the matter has not been before the people since 1851. The State Constitution prohibits such an enterprise.

IOWA

There was no state owned bank established in Iowa during territorial days and the first constitution provided that the General Assembly could provide for the organization of corporations "except with bank privileges, the creation of which is prohibited." When the new constitution was written in 1857, however, provision was made for the organization of banks. In 1858, the legislature passed an act; incorporated the State Bank of Iowa, with a limit of thirty branches, but with capital from private sources. The parent bank was neither a bank of issue nor deposit. It transacted no business except with the branches. Its records were to be kept open for the inspection of the General Assembly, the Governor, or a Committee appointed by the As-

sembly. Fifty per cent of the capital had to be paid in before commencing business, and the balance a short time thereafter. When the National Bank Act went into effect, with a heavy tax on circulating notes of state banks, steps were taken to wind up the affairs of the State Bank of Iowa. Most of the branches at once became national banks, and no noteholder or depositor lost any funds whatever, the branch at Davenport becoming the first national bank in the United States. As late as 1863, the only banks in the state were branches of this state bank. There is some sentiment in Iowa today for a state owned bank, not so much along the line of the pioneer state institution, as for a central bank to handle deposits of the state and its municipal subdivisions.

The state law requires payment of 2% interest on 90% of the daily average balance of public funds, except during April and October, when the interest rate is 1%. The inability of private banks to handle these deposits and invest them so that this rate of interest could be received has led to their refusal to accept such funds. The interest law cannot be repealed because the state also has an act which provides that the interest received shall go into the hands of the state treasurer as a sinking fund, from which the state treasurer is to pay municipal subdivisions throughout the state for public funds lost in state banks which closed. This fund is now in the red some \$18,000,000, and a state central bank which would pay this interest is therefore being agitated. The Governor has suggested some such measure to handle these funds, and in each of the last two legislatures a measure has been presented embodying these ideas. A state banking system has also been proposed to protect the state against the aggressiveness of the Federal Government in centralizing banks through the Federal Reserve System or the FDIC. There are constitutional obstacles to the successful establishment of such a bank.

Still another bill, proposing a State Bank of Iowa was introduced in the 1935 legislature. No capital was provided, but the state would guarantee all deposits. The state and all political subdivisions would be compelled to place their funds in this bank and private deposits would also be accepted. Six directors would be appointed by the Governor, with the State Treasurer a director ex-officio and Board Chairman. The bank could loan to

the state and its political subdivisions on ample security with no rate specified and to individuals on first mortgages at not more than 2½%. This bill failed to pass.

KANSAS

Neither during territorial days nor since statehood has Kansas engaged in the banking business, although at various times a state reserve bank has been considered in the legislature. A law permitting the organization of such an institution has always failed. There is no substantial sentiment for such a bank there at the present time. The constitution provides that the state shall not be a stockholder in any banking institution, this being adopted by the electorate in 1861, reaffirmed in 1880, and resubmitted in 1934. The repeal thereof suggested in 1934 was defeated by approximately 100,000 majority.

KENTUCKY

In 1802 a charter granted to the Kentucky Insurance Company carried with it the right to issue notes. The success of the banking business thus carried on led the legislature to pass an act making possible the incorporation of the Bank of Kentucky in December, 1806. Of the million dollars capital, one-half was to be held by the state, which had the right to name the president and six of the twelve directors. It should be noted that the legislature had the right to increase the number of directors from twelve to twenty-four, and the minority could therefore be outvoted by a politically appointed majority. Accordingly, acts of the legislature for this and that, many of which violated the original charter, were harmful in the extreme. In 1815, the legislature increased the capital stock to \$3,000,000 and in 1817 legalized an agreement which had been entered into between the mother bank and its 13 branches, that neither would be bound to take the notes of the other. The charter was finally repealed in 1822, with the state holding \$586,400 of its capital. Late in 1820, the state legislature had chartered for 20 years the Bank of the Commonwealth of Kentucky, with \$2,000,000 capital and a charter provision that it should be exclusively the property of the commonwealth. One-half the profits were to be devoted to public instruction.

Circulating notes of the Bank of the Commonwealth depreciated substantially. Court contests followed relative to the constitutionality of the act incorporating the bank, and when the Supreme Court held it unconstitutional and the notes issued were held not to be liabilities of the state, the bank closed in 1830. When the charter expired in 1841, it was not renewed. Between 1833 and 1835, the Bank of Louisville, the Bank of Kentucky, and the Northern Bank of Kentucky were organized. In 1838, the state owned 10,000 shares in the latter. Of the \$5,000,000 capital of the Bank of Kentucky, \$2,000,000 was reserved for the state, which reduced its stock to \$1,000,000 in 1843. Three directors were chosen by the state, and in 1877, after surviving the Civil War, the bank purchased the remainder of the state-owned stock.

LOUISIANA

The Commercial Bank of New Orleans, chartered in 1813, reserved one-sixth of its capital to the state. In 1818, Louisiana authorized a subscription of \$500,000 toward the \$2,000,000 capital of the Louisiana State Bank. The state was to appoint one-third of the eighteen directors, and the bank was to pay a bonus of \$100,000 to the state, the latter in consideration of the promise that forever the stock and real estate of the bank should be exempt from taxation. This bonus and exemption were part of subsequent charters, and only \$100,000 was ever actually subscribed to the capital. This institution therefore can hardly be called a state bank.

In 1824, the Bank of Louisiana was chartered, capital stock \$4,000,000, one-half of which was subscribed by the state, through a bond issue. The interest on the bonds was supposed to be paid from bank dividends. In 1844, the State Treasurer was authorized to sell 12,000 shares of Bank of Louisiana stock, and the remainder of the stock was also sold late in that year, the proceeds being used for retirement of bonds falling due. All these bonds therefore were retired by the bank. In 1832, the Union Bank of Louisiana was incorporated, with a capital of \$7,000,000. This was similar to the Union Banks in other states, in which the subscribers to stock paid nothing, the actual capital arising from the proceeds of the \$7,000,000 in bonds issued by the state. One-half of the twelve directors were appointed by

the Governor. This bank failed in 1842, and although liquidation was slow and difficult, by 1853, liquidation had realized enough to pay these bonds. The Consolidated Association also received an issue of state bonds in the amount of \$2,400,000 and the Citizens Bank \$8,000,000, of which \$7,188,000 were sold. These organizations were on exactly the same basis as the Union Bank. Both these institutions went into liquidation in 1842. Ten years later the Citizens Bank was reorganized, but the state in that year definitely withdrew, through a clause in its constitution, from the banking business.

By the time of the panic of 1837, sixteen banking organizations were located at New Orleans, with 31 branches scattered throughout the state, thirteen of them created since 1828. One of these organizations operated the city water works, another the gas works, and another ran a railroad, while two of the largest hotels in New Orleans were operated by banks. The state had issued nineteen million dollars above noted in bonds, largely sold in Europe to aid these banking institutions. By 1844, but six of these institutions were left. A stringent banking act was passed in 1842, and the surviving banks accepted its provisions, became solvent, and paid the state bonds which had been issued to them. By 1857, there were nine banks operating, five of the largest maintained specie payments on both deposits and circulation throughout the depression, and another suspended deposit payment for less than three weeks. Provisions of the Louisiana Bank law were rather generally recommended for adoption in a number of other states.

MAINE

So far as the records show, the State of Maine has never engaged in the banking business. While the state constitution does not directly prohibit engaging in such enterprises, there is a statutory provision which by implication would so act.

MARYLAND

Practically all the charters issued in the early history of the state carried a provision for subscription to stock on the part of the state itself, and a provision for appointment of directors on

the basis of two whenever the state held \$66,000 in stock. Two hundred and twenty shares out of 600 reserved were taken in the Bank of Baltimore as early as 1803.

The Mechanics Bank of Baltimore, chartered in 1806, had capital of \$1,000,000, of which \$94,625 was paid in by the state. Apparently the Bank of Maryland was the only bank organized up to 1806 in which the state was not a stockholder.

In 1811, it owned stock in each Baltimore bank and in three country banks, but thereafter ceased to make subscriptions, the amount held at that time totaling \$540,000. The directors to which it was entitled were elected by the General Assembly. About 1830, an active campaign was put under way to establish a bank under the direct control of the state. Although a legislative committee was appointed which made careful investigation and reported favorably, a measure providing for a state bank lost in the legislature. The bill, revived for several legislative sessions, was never enacted. While there is neither constitutional nor statutory prohibition regarding the state engaging in the banking business, no sentiment exists for it at this time.

MASSACHUSETTS

Massachusetts entered the banking business first in 1714, when 50,000 pounds sterling in bills was issued and placed in the hands of trustees to be loaned out at 5% on real estate mortgages in sums of 50 to 500 pounds sterling. An additional 100,000 pounds sterling was issued in 1716, and in 1721, another 50,000 pounds sterling.

The action of the British Parliament in 1740 whereby companies that had for their purpose the issuing of paper money were prohibited from organizing, caused the winding up of the affairs of the "banks" thus started.

When the Union Bank was started in Boston in 1793, the state retained the right to subscribe for one-third of the capital of \$1,200,000. By 1812, the state owned \$1,000,000 of bank stock, the same provisions having been included and made use

of in other charters. Apparently the state shortly retired from the business of banking and from then until the 1935 legislative session, the matter had not been before the commonwealth.

A measure was then introduced in the House at the request of the State Executive Committee of the Socialist Party for the establishing of a commercial bank to be owned and operated by the commonwealth. The measure would have repealed the charter of every commercial banking institution and the banking commissioner would have been directed to take charge of each one, liquidate its affairs, and establish the Bank of the Commonwealth of Massachusetts in Boston with such branches as the Governor might approve. The capital of the bank was to be provided through the sale of bonds of an undetermined amount, and the bank was to be the depository of all state, county, and municipal funds of every nature and description. Loans would have been made to home owners, business men, farmers, or others with a rate of interest such as would pay the operating expenses of the bank, establish reserves, and pay off the bonds issued as the bank capital. The bill failed of passage. There is no specific statutory or constitutional provision against the state engaging in this type of business.

MICHIGAN

Under the territorial government, a bank was organized at Detroit, in 1806, with a capital of \$400,000, to which territorial Governor Hunt subscribed ten shares on behalf of the territory. The Michigan State Bank was incorporated in 1835, and was expected to take control of the banking business of the state. The cashier of the bank was made fiscal agent for the state. Apparently, however, the state owned no stock in this bank. An attempt was made in 1839, prompted by the success in Indiana, to inaugurate the State Bank of Michigan, with a capital of \$2,000,000. The charter was authorized, but the capital was not obtained, and the bank never went into business. The constitution of the state is silent, as are the statutes of the state relative to the commonwealth engaging in the banking business. There is no substantial sentiment for such an institution.

MINNESOTA

About 1854, there was a movement to establish a Bank of Minnesota, which, however, failed, and in the Bank of the State of Minnesota, organized in 1858, apparently no stock was owned by the state government.

Proposals were made in the 1931, 1933, and 1935 legislatures for a state central bank to control public funds. There is some sentiment throughout the state for an institution of this kind, though it has not been sufficiently strong to compel the legislature to enact such a measure. The statutory prohibition against the state engaging in the banking business was repealed in 1933. The proposal in 1935 was given some impetus through a recommendation from Governor Olson in his message to the legislature that a central bank of deposit be established, the same to be the only legal depository for funds of the state and its municipal subdivisions.

In March 1935, still another bill for a Minnesota State Bank made its appearance in the legislature. It was proposed with a capital of \$3,000,000, two-thirds owned by the state, and one-third by state chartered banks, which would be compelled to subscribe thereto, 5% of their own capital. The bank would be the compulsory depository of state funds and all public funds of municipal subdivisions, and would be governed by a board of seven, three elected by the member banks, the Commissioner of Banks, and three appointed by the Governor, one of whom would be the manager. Although the preface to the bill indicated it was aimed at "group banking", and any concentration of banking, the bill would centralize deposits of all state chartered banks and the policies of the bank would be dominated by the state government. The bill failed to pass.

MISSISSIPPI

The Bank of Mississippi, the first bank to be organized in the state, was chartered by the territorial government in 1809 at Natchez, and operated as a private corporation until 1818, when it was created into a state bank with a capital of \$3,000,000, of which the state was to subscribe one-quarter

and appoint one-third of the directors. The charter was to continue until 1840, and no other banking institution was to be incorporated by the state in the meantime. The constitution of 1817 had provided that at least one-fourth of the capital of any bank must be reserved for state subscription. In 1830, in spite of the fact that no complaint had been made of the institution, the legislature disregarded the above pledge and chartered the Planters Bank of Mississippi, with capital of \$3,000,000, later increased to \$4,000,000, of which the state subscribed one-half and issued \$2,000,000 in bonds in payment therefor. A majority of the directors were appointed by the state government. The managers of the Natchez Bank at that time decided to wind up their affairs. In 1839, the state transferred its interest in this bank to the Mississippi Railroad Co. The Mississippi Union Bank was chartered in 1838, with a capital of \$15,500,000. Fifteen million dollars in bonds were to be issued, and loaned to the bank. Ten days after the passage of the original act, another was passed, requiring the Governor to subscribe for stock on behalf of the state, amounting to 50,000 shares. Branches in various districts throughout the state were authorized, but the establishment thereof was not pushed. Although only \$5,000,000 in bonds was issued to the Union Bank, by 1841, both that issue and the amount issued to the Planters Bank, and succeeded by the Mississippi Railroad Co., had gone in default. The bank went into liquidation late in 1841, having been the center of controversy in state politics since its organization. The repudiation of the bank bonds was the principal factor in the election of November, 1841, the candidate favoring repudiation winning the election.

The 1842 legislature passed the formal act of repudiation, and although the matter was taken to court and the state held liable in 1853, neither principal nor interest has been paid. By the state constitution, the legislature is denied power to pay the bonds. This did not cover the bonds issued for the Planters' Bank capital. In 1852, the voters of the state refused to submit to a direct tax for the purpose of paying these bonds, and the state constitution now prohibits their payment also. Not since 1842, has the electorate or the state legislature had the matter of a state owned bank before them.

MISSOURI

Although during territorial days, two banks had been created in Missouri, both had passed out of business by about 1819. Banking of a kind was carried on in the territory and state prior to 1837, but the withdrawal of the branch of the Second Bank of the United States located in St. Louis prompted the state legislature to create the Bank of the State of Missouri. The Missouri constitution of 1820 carried a proviso for the incorporation of one banking company, and no more. It also provided that the maximum capital should be \$5,000,000, and at least one-half reserved to the state. The legislature in 1821 passed an act establishing loan offices, which through the state treasury issued \$200,000 in certificates. Certain property of the state was pledged for their redemption. The United States Supreme Court finally decided that these were "bills of credit", and that their issuance was therefore unconstitutional. The next attempt on the part of the state was in 1837, when the Bank of the State of Missouri was chartered. Five branches were established, and the state subscribed to half its capital stock. It issued bills which were always redeemed at par. As late as 1856, it is reported that the only incorporated banks in the state transacting a general banking business were the Bank of the State of Missouri, and its five branches. Of the capital of \$1,215,000, \$954,000 was at that time owned by the state. By 1863, the state capital had been increased to \$1,086,300, and aggregate capital to \$3,400,000. Establishment of other banks resulted in a restriction of the business for the state bank, the constitutional prohibition against other banks having been removed in 1854. The new state constitution in 1865 required that the legislature provide for the sale of the stock owned by the state. This was done, the purchasers converting the institution into a national bank. It is interesting to note that the conservative management of this bank made the notes thereof so valuable that in the Fifty's, after gold had been discovered in California, a gang of counterfeiters took advantage of the popularity of the Bank of Missouri paper money and struck off counterfeits thereof, which were freely taken in California by miners, merchants, and private bankers. One package of them of \$15,000, for which a premium in gold had been paid in San Francisco, resulted in a loss of that amount to a wealthy citizen of St. Louis.

EXHIBIT 3 300

The constitution of 1875 provided that no state bank should thereafter be created nor should the state own or be liable for stock in any banking corporation. There is no substantial sentiment for such an institution at the present time.

MONTANA

Until recently, there has been practically no agitation for a state owned bank in Montana. During the 1935 legislature, however, such a measure was proposed, creating the Bank of Montana, to be operated by the state. The governing body of five was to be composed of the Governor, Secretary of State, Attorney General, State Treasurer, and Commissioner of State Lands. One hundred thousand dollars was to be appropriated as the capital, and the bank was to be compulsory custodian of all state, county, municipal and all other public funds, with a proviso in the act that all deposits were guaranteed by the state. No guaranty fund, however, was set up. The measure was presented in the House and defeated by a vote of 55 to 40.

NEBRASKA

There was no state owned bank in Nebraska. The criminal code of the first legislative session in 1855 providing that if any person should subscribe or become interested in a company formed for the purpose of issuing paper to circulate as money, he should be punished by one year's imprisonment or a fine of not more than \$1,000.

While the state itself has never engaged in the banking business, there have been some attempts at various legislatures to pass some act of that kind. In 1933, a measure was sponsored by the Governor and a similar bill was introduced in the 1935 legislature. Neither the state constitution nor statutes prohibit such a measure. The bill in the 1935 legislature provided for the establishing of the Bank of Nebraska to engage in the banking business provided the state and national banks doing business in Nebraska had not applied for and become depositories of all public funds of the state and its municipal subdivisions within

23 days of the passage of the act. No capital was provided but \$100,000 was appropriated as a revolving fund. The bank would receive only public funds on the limited basis above set out. As this is written, sentiment in Nebraska is to the effect that the act will not pass.

NEVADA

The state constitution prohibits the state engaging in the banking business. Neither during territorial days nor since statehood has such an enterprise been established, and neither the electorate nor the legislature has ever had the proposition before them.

NEW HAMPSHIRE

There is no sentiment at the present time for a state bank. There was a company formed about 1735, which issued notes much on the plan of the Merchants Association of Boston. These notes, however, were prohibited from circulating in Massachusetts. The first bank in the state was the New Hampshire Bank, incorporated at Portsmouth in 1792. It had a capital of \$160,000, and while it was the only bank in the state until after 1800, the records do not indicate whether the state held any capital therein. The original constitution did not prohibit the state engaging in banking, but about the middle of the last century, a proviso was inserted which prohibits any town, loaning or giving money or credit "for the benefit of any corporation having for its object a dividend of profits or to in any way aid the same by taking its stock or bonds."

NEW JERSEY

As noted elsewhere, New Jersey along with other Colonies, issued paper money. Inasmuch as a substantial quantity of this was for loans on real estate, they were known as "loan banks". Proximity of Philadelphia and New York seems to have delayed organization of incorporated banks until after 1800.

The first banks organized in this state provided for a bonus to be paid to the state for the privilege of obtaining a banking

EXHIBIT 3 - 1914

charter. The Trenton Banking Co. offered a bonus to the state which was refused, but the state reserved a right to subscribe to stock, \$24,000 being subscribed in 1811 for the benefit of the public schools. The Newark Banking and Insurance Co., chartered in 1804, paid the state a bonus of about \$1500 for the privilege of operating. A bill was presented in the legislature in 1812, providing for the establishment of state banks at Camden, Trenton, New Brunswick, Elizabeth, Newark, and Morris, now Morristown. This bill provided that half the capital in each of these banks should be reserved for the state. The state owns no bank stock today, and there is no substantial sentiment for a state owned bank at this time, although a bill was presented in the 1934 legislature creating a Central Reserve Bank.

The bill set up the Central Reserve Bank of New Jersey, and banks authorized to do business by the state would have been required to become stockholders therein. Three directors, the Governor, Commissioner of Finance, and Commissioner of Banking and Insurance, and nine others, four appointed by the Governor or the legislature, and five by the member banks would constitute the Board. Five million dollars capital was proposed, half common and half preferred stock, the common stock to be held only by the State of New Jersey and the member banks, but a majority to be held by the state. The plan contemplated that each state bank would become a shareholder, irrespective of whether or not they held Federal Reserve membership. Funds of the state and its political subdivisions were to be deposited therein. The bill also contemplated setting up of an insurance fund to insure the deposits of the member banks. The act failed of passage.

NEW MEXICO

Neither the state nor territory have ever engaged in the banking business. There is no substantial sentiment for such a bank at the present time, nor has there ever been any. The state constitution neither prohibits nor authorizes such an institution.

NEW YORK

The Bank of New York, doing business under articles of association drawn by Alexander Hamilton, and chartered in 1791, had a capital of \$900,000, and through a subscription by the State of New York, added 500 shares, and \$50,000 capital, which was of course owned by the state. In an act extending its corporate existence passed in 1813, the Comptroller of the State was authorized to subscribe an additional \$15,000 in stock for the benefit of the common school fund. Bank charters granted from 1791 to 1812 generally contained provisions authorizing the colleges to subscribe for stock, and on some occasions, the state itself was so authorized. For example, the Mechanics Bank, New York City, organized in 1810, reserved to the state the privilege of subscribing for one-sixth of the capital. When the Bank of America was chartered in 1812, the state did not subscribe for stock, but the bank was to pay \$400,000 to the state as a bonus, and to loan the state at any time it might require, a million dollars at 5%, and an additional million dollars at 6%. Both bonus and loan requirements were remitted within the next few years. In 1833, the State of New York owned \$85,000 of stock in institutions which had become insolvent.

Since the first part of the last century, New York has not engaged in banking as a state, nor has the question, at least recently, been seriously considered. There is no sentiment for such a set-up now, although the constitution and statutes are silent on the question of authority to do so.

NORTH CAROLINA

Paper money was issued by the Colony, but apparently no corporate banking institutions were established until after the turn of the century. The Bank of Cape Fear, chartered in 1804, had a capital of \$250,000, with \$25,000 thereof reserved for the state. The Bank of Newbern, chartered the same year, with a capital of \$200,000, also had \$25,000 reserved for the state. The act creating the State Bank of North Carolina was passed in 1810. It had capital of \$1,600,000, with the principal office in Raleigh, and six branches. Two hundred and fifty thousand dollars of the stock was reserved for the state, with the dividends on the stock to be used for paying the outstanding

EXHIBIT 6

paper money issued in 1783 and 1785. In 1814, the charters of the first two banks were extended to 1835, and the capital of the Bank of Cape Fear was enlarged by \$525,000, and State Bank of Newbern by \$575,000. An additional \$100,000 capital in each was reserved for the state, \$18,000 of this to be issued without the state paying anything therefor, as consideration for the extended charter. A further requirement was that the banks would be required to make loans to the state not exceeding one-tenth of their capital stock. In 1828, the State Treasurer was by resolution of the Assembly prohibited from making any further investment of state funds in bank stock, but a short time previous thereto he had purchased additional shares in all three banks. In 1832, an act was passed to establish the Bank of North Carolina. It was, however, never organized, but in 1833, the Bank of the State of North Carolina was chartered, with one and a half million dollars capital, two-fifths of this reserved to the state. During the session of 1836-37, the charter of the Bank of Cape Fear was continued to 1850, the capital increased to 1½ million dollars if the stockholders desired, but the state allowed \$300,000 of the increase. In 1858-59, the General Assembly chartered the Bank of North Carolina as the successor to the Bank of the State of North Carolina, which had previously succeeded the State Bank of North Carolina, chartered in 1810. The capital was 2½ million dollars, \$500,000 of which was reserved for the school fund, and \$200,000 for the university. The Civil War ended the career of this bank. Although its stockholders lost their investment, it was contended and with some substantial ground, that the bank was founded on sound principles and would, except for the war, have been a blessing to the community. Although the state constitution does not prohibit such an organization, there is no interest whatever in a state owned bank at this time.

NORTH DAKOTA

Prior to 1919, the state had not engaged in the banking business. The legislature of that year created the Industrial Commission, and authorized it to operate the Bank of North Dakota, created by the same legislature. The Industrial Commission is composed of Governor, Attorney General, and Commissioner of

Agriculture and Labor. The bank was set up at the same time the Non-Partisan League (the controlling political power) started the state in the Mill and Elevator, Co-operative Store, and similar commercial enterprises.

Two million dollars capital was furnished the bank through issuing the same amount in state bonds. All funds of the state *must* be kept in the bank and although deposit of funds of political subdivisions was compulsory at first, it was made optional in 1923. Private and corporate funds may also be accepted. The bank is not a member of the FDIC, but the law pledges the faith of the state as security for deposits.

Loans to the state and state enterprises and to political subdivisions were authorized. Loans to private individuals can be made on mortgage security. A series of "Real Estate Bonds" have been issued, the bonds being sold by the state and funds held by the State Treasurer. Mortgages taken as security on loans made by the bank are then pledged with the State Treasurer as security for the bonds which are general obligations of the state, and the State Treasurer then turns the funds represented thereby over to the bank. Loans could not be made to private individuals, but large deposits of bank funds were made in banks favored or controlled by the League, and these banks then could and did loan to private individuals. After two years operation, rumblings of dissatisfaction with operation of the Bank were heard and the House of Representatives of the 1921 legislature appointed a special committee to investigate the bank, its operation, and affiliation of bank officers and state officers with League and state enterprises. The report is contained on pages 925-978 of the Journal of the House of Representatives of the 1921 legislative session, with supporting testimony given before the committee following. Extracts follow:

"A fair conclusion is that A. C. Townley and Wm. Lemke exercised dominating and controlling influence over the original organization of the bank and its subsequent operations. This conclusion is fully verified by the record, * * * which discloses that the resignation of the first manager was due to his refusal to comply with the directions of the aforementioned persons to divert the funds of the Bank of North Dakota to the Scandinavian-American Bank of Fargo.

EXHIBIT 3

"In financing the various League concerns, and the political campaigns conducted by the League, Messrs. Lemke and Townley approved a scheme whereby they obtained notes from farmers throughout the state by way of accommodation and in exchange for the individual notes of Townley and League corporations. In addition thereto, the farmers were induced to give their post dated checks for like purposes. This accommodation paper was accumulated in large amounts and a great flood of it was placed in the various banks in the state affiliated with the League as collateral to loans made to the League and its subordinate and kindred corporations.

"The most striking and typical example of this practice is to be found in the Scandinavian-American Bank of Fargo, where, the evidence discloses, many thousands of dollars of farmers' accommodation notes and a large quantity and amount of post-dated checks were held as collateral to excessive loans to the Consumers' Stores Co. and the League Exchange."

The Committee went on to state:

"The examiners find from the record that during the month of February, 1921, the account of the State Treasurer with the Bank of North Dakota amounted to approximately 3 million dollars. While this balance was maintained, the State Treasurer drew checks upon the Bank of North Dakota against this account in various small amounts. These checks were refused payment by the Bank of North Dakota, and in lieu of payment, * * * the checks were registered as "presented for payment, not paid for lack of funds". Such failure to pay current checks constitutes an act of insolvency. If any other bank attempted similar tactics, it would at once be incumbent upon the State Examiner to close it without delay."

The Committee listed six "permanent fallacies in the organization" and concluded their report with some rather strong statements, two of which are:

"These impractical theorists have launched the State into an orgy of financial excesses and delirium of socialistic experimentation, born in hate and nurtured in prejudice, the

results of which are such that it will require years of conservative, practical administration of public affairs to eliminate the nefarious consequences resultant therefrom."

"The Committee recommends that the State confine its business activities to those matters which are, in their nature at least, quasi governmental in character, that it awake from its socialistic dream of empire, independent of its neighboring states; that it brand as "quack" the remedies for industrial injustice that have been recommended as the panacea for all ills, and confine itself to a specific remedy for each specific injustice that may become apparent in the body politic, that it divorce itself from the false prophets whose leadership has ousted it from a place of honor among the states of the Union * * * ."

From the messages of Governor Geo. F. Shafer to the 1929 and 1933 legislatures, a good picture of the bank's situation may be gained.

From the message of 1929:

"At the time the present management took over the operation of the bank in December 1921, it was in deplorable condition. Heavy operating losses had been sustained, and many millions of public funds were tied up in frozen loans and re-deposits in closed banks, much of which was either unsecured or inadequately secured."

From the message of 1933:

"On July 1, 1919, the state issued \$2,000,000 of unsecured bonds, bearing interest at the rate of 5 per cent, to provide the capital for the Bank of North Dakota, which was organized in August of that year. \$1,000,000 of these bonds matured on July 1, 1929, ten years after issuance, and were paid when due entirely by taxation. The second installment of \$1,000,000 of such bonds will mature on July 1, 1934.

"There is now in the bank bond sinking fund in the hands of the state treasurer, the sum of \$1,000,000, the full amount required to retire this issue when due. \$300,000 of this amount has been provided from taxation and \$700,000 has been paid over to the state treasurer by the Bank of

LIBRARY

North Dakota from earnings. The annual interest on this installment of bank bonds, amounting to \$50,000, has been paid by the Bank of North Dakota from earnings since 1929. Prior to that date, the annual interest on the total of \$2,000,000, amounting to \$100,000, was paid by taxation."

From the annual report of the State Treasurer for the year ending June 30, 1934, a tabulation of the bonded indebtedness of the state shows a total of \$41,917,200, all of which are for State Bank, Mill and Elevator, or Real Estate loans. Since that time, the amount has been reduced by paying as they fell due, \$2,000,400 worth.

In addition to the bonds for bank capital which were retired by taxation as indicated by Governor Shafer, a general property tax levy of $\frac{1}{2}$ mill was made in 1933 to pay interest and sinking fund on Real Estate Bonds, $\frac{8}{10}$ of a mill in 1934 and the 1935 legislature authorized further levies of $\frac{1}{2}$ mill for 1935 and 1936. Altogether, about 12 million dollars has been raised by direct taxation to pay losses of the bank, and losses of the Mill and Elevator and rural credits. Since 1933, in addition to the funds raised by general taxation, motor vehicle registration fees have been diverted to the Real Estate Bond Interest Fund. In the fiscal year 1933-34, \$900,000 was thus diverted and between June 30, 1934, and December 31, 1934, another \$600,000 was similarly used.

Foreclosures have not been averted. On January 1, 1935, the state held title to some 2,200 farms on which they had foreclosed in spite of a lenient policy. Many loans have been refinanced through Federal agencies, the losses incurred thus far being about \$2,000,000, including both principal and interest. Real Estate loans are not now being made as the rates of the Federal Government are below those at which the state can issue bonds.

With the state taking the loss and the bank taking the profit, the bank shows a splendid cash position in its December 31, 1934 statement. On the other hand, the bank has paid to the state a total of \$1,117,318.88 out of earnings over the 15-year period to apply on bonds and interest. Bank proponents also claim credit for an interest reduction on farm loans of about $2\frac{1}{4}\%$ on \$280,000,000 of North Dakota farm mortgages, based on the rates prevailing before and after the bank got into operation.

In its December 31, 1934 statement, the bank showed deposits of \$26,527,045.85, all of which were public funds except \$3,824,267.96, representing deposits of individuals and banks, plus cashier's checks.

OHIO

The custom prevalent in Atlantic Seaboard states early in the last century of reserving a part of the stock in banks for the state, was also current in Ohio. The first record of such seems to be the Bank of Marietta, chartered in 1808 and which so reserved one-fifth of its capital. In 1816, the legislature chartered six new banks. Seven existing institutions were authorized to continue under the provisions of the same act, which included that each bank would reserve one share of stock for the state for every 25 of capital stock. In 1825, this stock was reinvested in the banks, and in lieu thereof, a tax on dividends was levied. An act of 1845 fixed the maximum bank capital for the state at slightly in excess of six million dollars, divided the state into twelve districts, and provided that the core of the state banking system was to be a State Bank, capitalized by private money, with branches throughout the state. Before its charter expired in 1866, the National Bank Act had been passed. The charter was therefore not renewed, and the bank wound up its affairs. Branches had a minimum capital of \$100,000, and some independent banks whose charters had expired became branches of the State Bank. Forty-one branches in all were organized throughout the state, with an approximate capital of \$4,500,000. These branches were real individual corporations under the supervision of the central bank officials. The latter did no banking business, but through it issued bank notes to the branches. The bank was completely successful. When the bank was winding up its business in 1866, the president made the following statements to the Board of Control: "The State Bank of Ohio has always proved equal to the trials it was called upon to meet. The people have been supplied with a circulating medium which commanded their confidence, and by the use of which no one ever lost a dollar. Stockholders received substantial dividends throughout the existence of the bank, and were repaid in full upon liquidation." The Ohio constitution and statutes are silent on the question of State ownership of banks.

OKLAHOMA

The state has never engaged in the banking business, and there is no substantial sentiment for such a plan today. Neither the electorate nor the legislature has ever had the proposition before them. The state constitution prohibits the state engaging in the banking business.

OREGON

The state, neither during territorial days nor since statehood has engaged in the banking business. Such a venture is prohibited specifically, both in the state constitution and by statute, and the state constitution further makes illegal the pledge of the credit of the state for more than \$50,000, except in time of war. There is some sentiment in the State Grange, and some other quarters for a state owned and operated bank. A proposal has been made in each of the last two legislative sessions, and an attempt was made by initiative to get such a plan on the ballot in November 1934. Each attempt has met with failure. The latest plan contemplated establishing a bank without capital. A guarantee of deposits was carried in the bill, with no guaranty fund, nor a method of setting one up. The bank was to hold all state funds, and funds of all political sub-divisions, court funds, etc., and to loan principally against real estate. Other funds could, however be accepted. A measure carrying similar provisions was presented in the 1935 Legislature but was decisively defeated.

PENNSYLVANIA

Pennsylvania was another of the Colonies that issued paper money through "loan banks". Fifteen thousand pounds sterling was issued and loaned out in 1723. Bills were made legal tender and their retirement provided for by requiring that interest and $\frac{1}{8}$ of the principal be paid annually. In 1793, the state subscribed for one-third of the capital of the Bank of Pennsylvania, and within a few years it obtained as dividends on bank shares it held, nearly enough to pay all its expenses. Branches were established at Harrisburg, Reading, Easton, Lancaster, and Pittsburgh. These branches discontinued about 1810, but at that time the state held a million dollars worth of the stock it had sub-

scribed, and later raised its stockholdings to a million and a half. An act of 1810, after the bank charter had been extended for 20 years, provided that whenever money in the state treasury exceeded \$30,000, the Governor should invest the surplus in \$5,000 units in the stock of the Bank of Pennsylvania.

The State also owned stock in the Farmers and Mechanics Bank of Philadelphia, chartered in 1809, and in the Philadelphia Bank, chartered in 1804. The latter charter permitted the state to subscribe for \$300,000 out of the total of \$2,000,000 capital, with a further subscription privilege of \$200,000 at the end of four years, and a similar amount at the end of eight years. In Pennsylvania, as in some other states, bonuses were paid for the granting of charters. For instance, when the Bank of North America had its charter renewed for ten years in 1814, it paid the state \$120,000 as a bonus for the renewal thereof. Most of these banks earned good dividends, for instance, in 1813, the state received nearly \$200,000 from that source, or about two-fifths of the entire state revenue. However, all was not rosy for these institutions. In the Bank of Pennsylvania, six of the 22 directors were appointed by the state, forming a block which worked continually in opposition to the majority. When complaint was made in 1829 that the Bank of Pennsylvania did not loan as much as was desired to the state, it was admitted that the state directors introduced a "pertinacious, persevering, and indiscriminating opposition to almost any prominent measure which is proposed by directors elected by stockholders." The state sold all its bank stock in 1843 and since that time has not engaged in the banking business. There is no sentiment for a state-owned bank today. Neither the electorate nor the legislature has ever had the proposition before them. Apparently there is no prohibition in the constitution against the state engaging in the banking business, but under the 1933 banking code appears a requirement that the incorporators shall be "natural persons".

RHODE ISLAND

In 1715, the colony issued 40,000 pounds sterling in paper money, which was known as the first bank. A second bank of 40,000 pounds sterling was issued in 1721, and other issues known as banks were put out from time to time. The state never subscribed for bank stock, but as in some other New England

states, bought such stock for school funds. In the words of a prominent state official, the matter of a state owned bank is simply an unheard of proposition in Rhode Island today. The matter has never been before the electorate, nor has there ever been any substantial sentiment for such a proposition. There is no mention of it either in the statutes or in the constitution.

SOUTH CAROLINA

The only bank organized during proprietary government days was the Land and Loan Bank of the Carolinas, located at Charlestown, chartered in 1712 with a perpetual charter, which carried with it the privilege of issuing bills to be forever the legal money of the country. 100,000 pounds sterling of currency was immediately printed and loaned out at 10% to such as could give security. Although the bills depreciated in value and the exchange rate on London was eight to one, this bank which lasted until destroyed by the Revolutionary War, is said to have been of great benefit in building the Colony.

In 1792, the new state chartered the Bank of South Carolina, and in 1804, the Legislature subscribed to \$300,000 of its capital. To the Southwestern Railroad, organized in 1836 and 1837, the State of South Carolina in 1839 subscribed \$500,000 out of the \$6,000,000 capitalization. In the meantime, the Bank of the State of South Carolina was chartered in 1812 to relieve financial distress, entirely owned by the state and for which it served as fiscal agent. The faith of the state was pledged to support the bank and make good all losses. Its charter was to run until 1836, and as a privilege of doing business, it was to pay interest on the state debt. The State of South Carolina, as noted above, was the sole owner, and although its capital originally was about \$150,000, it was increased by 1820 to approximately \$1,200,000, and by 1828, had paid into the state treasury more than \$1,315,000. The charter of the bank after this successful showing was renewed until 1856, and prior to expiration was extended to 1871. In 1868, the legislature, after the bank had successfully weathered the Civil War, passed an act to close it, and in 1870, it was placed in the hands of the receivers. There is no sentiment in the state for any such plan at the present time.

SOUTH DAKOTA

In the 1933 legislature, a plan was introduced to create the South Dakota Reserve Bank. The bill received an unfavorable report and was killed in the Senate where it had originated. There is some slight sentiment for such a plan at the present time. A previous plan which was proposed in 1921 by initiative petition, lost out with a vote of 33,000 for the act and 123,000 against.

This proposal carried with it a state bond issue of \$2,000,000 with the bonds to be turned over to the bank for their own purchase or to be sold by them to investors, and also provided that if earnings of the bank were insufficient to pay interest and sinking fund requirements on the bonds, the Tax Commission would make a levy to cover the difference. It was supposed to be custodian of all public funds of the state and all municipal subdivisions, and to establish branches throughout the state. The 1933 proposal contemplated a reserve bank of which every state chartered institution would be a compulsory member. The Governor, subject to confirmation by the state Senate, would have the authority to appoint a majority of the directors. The capital was to be provided by the member banks in proportion to their capital and surplus, and any net income after dividends and expenses was to go to the state as a franchise tax. All funds of the state were to be deposited in the bank, and funds of cities, towns, and other political subdivisions might be deposited in banks, members of the Reserve System, or in the bank itself. The act also attempted to authorize the Reserve Bank to issue its notes, which would be receivable for taxes, etc., and redeemed in lawful money of the United States on demand.

TENNESSEE

The Bank of the State of Tennessee, chartered in 1811, had a capital of \$400,000, with the state holding \$20,000 thereof, which it might withdraw at the end of ten years. This bank and its five branches failed within a few years.

In 1820, the State Bank of Tennessee was incorporated, with an authorized capital of \$1,000,000 to come from funds belonging to the state. A Board of Directors was appointed by the legislature, and from the sale of lands, the bank ultimately secured a capital of \$750,000. Agencies were established in every county

EXHIBIT 3

of the state, and the bank made the depository of all state funds. In 1832, after the bank got into trouble, the legislature abolished it, and ordered that all state funds be placed in the Union Bank of Tennessee, chartered in October 1832, with capital of \$3,500,000, all supplied by the state. This was obtained by the sale of state bonds, and five branches established. The state also had an interest in the Planters' Bank, chartered in 1833, with a capital of \$2,000,000, and with a head office at Nashville and six branches. In 1856, the state interest in the Union Bank of Tennessee was transferred to another Bank of Tennessee which had been chartered in 1838. This bank had an actual capital of about 3¼ million, all owned by the state, consisting of recoveries from the state bank, government funds, school funds, and some others. Its nominal capital, however, was \$5,000,000. This was a political organization, politically controlled, with directors appointed every two years by the state. The obligations placed upon this bank in the way of interest on internal improvement, school, and other bonds were too heavy for it to carry. The Governor in 1855 recommended that the affairs of the bank be wound up. The bank, however, continued until 1866, when the legislature passed an act requiring the Governor to appoint six directors to wind up its affairs. The holders of bank notes were finally paid in full, but the depositors received nothing. In 1875, still another attempt was made for state banking by reviving the Bank of Tennessee through an issue of \$5,000,000 in state bonds. The people of the state, however, did not look with favor on the attempt. There has been no agitation for a state owned bank in recent years, and the Constitution now prohibits the state engaging in the banking business.

TEXAS

Since statehood, Texas has not engaged in the banking business; however, in 1838, during the days of the republic, the President recommended the establishment of a national bank, founded on the credit of the Republic, to be controlled by the government, the directors to be elected by both houses of the Congress. The bill to incorporate the Bank of the Republic of Texas was introduced in 1839, but tabled in the Senate by the close vote of 16 to 14. The Commercial and Agricultural Bank started while

Texas was still a state in the Mexican Republic, was intended as a governmental bank of the Department of the Brazos. The Texas Congress in 1841 passed an act authorizing the projectors of that bank to issue \$30,000 of circulating money, but this act was shortly repealed.

The State Constitution of 1845, on which Texas was admitted to the Union, contained this statement, "No corporate body shall hereafter be created, renewed, or extended with banking or discounting privileges."

The matter of a state owned bank has not been before the electorate since. While the present Constitution and statutes are silent on the matter, there is no substantial sentiment for such an enterprise.

UTAH

There is no responsible sentiment for a state owned bank in Utah. The state has never engaged in the banking business, neither has the proposition ever been before the people or the legislature. Both by statute and state constitution, is the state prohibited from engaging in such an enterprise.

VERMONT

In 1806, the Vermont State Bank was chartered for the purpose of "securing for the state all the profits of the banking business". All the stock in the bank was owned by the state. The bank was to be managed by thirteen directors chosen by the legislature. One branch was established on either side of the mountains. Two other branches were established in 1807, and the bank in that year was made the depository of all funds of the state. Issuing of bills was limited in proportion to the amount of specie held, and fixed at three to one until specie amounted to \$300,000. In 1810, this was reduced to two times. By 1812, the Assembly became concerned over the solvency of the bank, one branch of which had already closed, and the legislature in that year assessed a land tax of 1 cent per acre, the funds received being used to redeem bills of the bank, whose affairs were to be closed as quickly as possible. All creditors other than the state were paid in full, but about \$230,000 of the bills which had been received by the state treasurer for taxes were never redeemed. Assets of the

bank which were not used for payment of creditors were about \$30,000, so the state apparently suffered a net loss of about \$200,000 through its banking effort. There is no substantial sentiment for a state owned bank in Vermont at this time. In recent years, the matter has not been suggested to the electorate or the legislature; however, neither the state constitution or the state statutes prohibit such an organization.

VIRGINIA

In 1755, the General Assembly of the Colony authorized the colonial treasury to issue 20,000 pounds sterling of treasury notes, and made them legal tender for everything "except his Majesty's quit rents". In August the plan had apparently worked so well that 4,000 pounds sterling more were issued to pay the rewards for Indians either killed or captured, and 20,000 pounds sterling to protect "His Majesty's subjects against the insults and encroachments of the French."

The notes depreciated rapidly in value. The following year 25,000 pounds sterling was issued, and in 1757, a still additional issue was made. Incidentally, counterfeiting of them was made a crime, punishable by death "without the benefit of clergy".

In the Bank of Virginia, incorporated by the General Assembly in 1804, the state subscribed to \$300,000 of the 1½ million dollars capital stock. The state then borrowed it back at 4%, payable in ten equal installments.

The Farmers' Bank, chartered in 1812, with a capital of \$2,000,000, had the state as a stockholder for 3,334 shares. Nine of the fifteen directors of the head office, and eight of the thirteen directors for each branch were to be elected by the legislature. Each branch issued its own notes, and was a complete bank, with all the functions necessary to meet the demands of the community in which it was located. No one lost anything in these old state banks. In the Bank of the Valley at Winchester, and the Northwestern Bank of Wheeling, both established in 1817, the Merchants and Mechanics Bank, also of Wheeling, 1834, the Exchange Bank of Norfolk, 1837, and several other banks chartered in the same year, with capital aggregating \$5,000,000, the state owned one-half. Practically every bank in Virginia went out of existence by the close of the Civil War, including these

banks above named, except the Northwestern Bank at Wheeling. Upon separation of Virginia and West Virginia, this bank took a national charter and became the National Bank of West Virginia, privately owned and today is the "oldest bank west of the Alleghanies".

WASHINGTON

There is some sentiment in Washington similar to that in Oregon for a state owned and operated bank. It received some impetus early in 1935 when State Treasurer Case suggested that the legislature pass such an act. The bill was introduced but did not get further than the Banking Committee of the House. It provided that at the general election in November 1936, there should be submitted to the electorate a new section to the Banking Law, which would provide that the legislature could authorize the state to engage in the banking business, and that the state in the conduct of the business should be liable for all deposits received. There is no statutory prohibition, but direct statutory authority would be necessary before the state could embark on such a program, and in addition the state constitution provides that the state may not obligate itself for more than \$400,000, except for an emergency such as riot or invasion.

WEST VIRGINIA

There has never been an attempt in West Virginia to set up a state owned bank, and the matter has not been presented to the electorate. Both by statute and by constitution, the state is prohibited from engaging in the banking business. (See also Virginia for history prior to separate statehood.)

WISCONSIN

The territorial constitution prohibited banking, and the legislature in granting charters to corporations invariably put in the clause, "Provided that nothing in this bill shall be construed as authorizing the business of banking." No state banks were organized, although an attempt was made to organize a State Bank of Wisconsin through the territorial government, but the approval thereof was not granted by Congress. The Constitutional

Convention in 1846 adopted an article prohibiting the organization of any banks of circulation, discount or deposits. The Constitutional Convention of 1847-48 adopted an article allowing banks to be organized under rigid restrictions, but no state bank system was ever attempted until recently. There has, however, in recent years been agitation for a state owned and operated bank. In 1931, the matter was presented to the legislature; was presented again in a special session that fall; and introduced again in the 1935 legislature. Three measures were introduced in the latter session, one of them providing a "state savings depository" which would accept both savings and commercial accounts from individuals with branches authorized throughout the state. Funds deposited with the state would be redeposited by the state in Wisconsin banks, on which 2¼% interest must be paid and collateral pledged to secure the same. The faith of the state would be pledged for payment of deposits made in the state bank, together with accrued interest. A companion bill introduced by the same sponsor provided for the establishment of the Bank of the State of Wisconsin at Madison, with the governor and state treasurer respectively the president and cashier. This bank would be the compulsory custodian of all state funds; could establish branch offices throughout the state, and would be specifically charged with the promotion of credit unions. Still a third bill would provide for a central state reserve bank, to be owned by the member banks, and providing that each state chartered bank and trust company must subscribe to stock in the central reserve bank, equal to 6% of its paid up capital and surplus. Optional membership would be provided for national banks "whose stock is not owned or controlled by foreign corporation, association, or trust, and which is not a member of any banking chain or group * * *". This bank would be the compulsory depository of all state, county, city, village, school, and other public funds.

WYOMING

The state has never engaged in the banking business, nor is there any substantial sentiment for such an organization at this time. The proposition has never been before the electorate, and neither in the constitution nor in the statutes is there any reference thereto.

Doubtless in most cases sincere, the enthusiastic sponsors of recent measures which would again put our states in the banking business, have painted a picture of what such enterprises would bring in the way of easier credit, together with returns to the public generally and municipalities specifically, that is not supported by these historical facts.

An unbiased survey of these facts brings out that: (1) depositors and bill holders suffered extremely heavy losses in these state banks; (2) investors in state bonds lost some \$65,000,000 principal and interest through repudiation and the reputation gained thereby took years to overcome; (3) the taxpayers in states where repudiation was not resorted to were 50 years in paying the losses incurred and in retiring bonds; (4) political management, which was impossible to avoid where the states sought to protect their capital invested, resulted disastrously in almost every case; (5) the most successful state banks were superseded by the National Banking System and in operation were central banks for control of policies only, with the actual banking units, branches thereof, privately capitalized and with non-political, private management; (6) the states which tried state banking, in spite of some successes, have the strongest constitutional provisions today, preventing other attempts; (7) of the states in which such recent proposals have been made only one (Iowa) has previously engaged therein, and Iowa had no capital investment in the previous bank which was organized as described in (5) above.

Mr. Crouch
3
SB 287

State-owned banks: New wine for old bottles?

What experience and history teach is this, that peoples and governments never have learned anything from history, or acted on principles deduced from it.

Georg Wilhelm Friedrich Hegel - *political philosopher*

Allocation of credit has caused perennial conflicts and controversies ever since the founding of our republic. Dissatisfaction with the market system's allocation of credit has brought forth demands for increased government control, planning, and intervention in the allocation of credit. Advocates contend, in general, that the private market economy—through the price mechanism—either has failed to or will not allocate sufficient credit and other resources toward certain “socially desirable investments” (e.g., housing, students, farmers, small businesses, and state and local governments). Others contend that any effort by the government to alter the allocation of credit has in the past—and would in the future—disrupt and destabilize the financial community; furthermore, the social costs of these efforts would exceed the benefits and would be “administrative nightmares.”

The methods most frequently discussed for altering credit flows may be placed in the following broad categories: (1) policies directed toward altering the overall *price* of credit (various tax and subsidy programs), (2) selective credit controls intended to limit and/or allocate the *quantity* of credit available (ceilings or quotas), and (3) the development and *alteration* of

financial institutions to achieve a more effective allocation of funds to the “priority sectors.”

This article focuses upon the third category, dealing primarily with a particular class of financial institution—state-owned banks. These are defined as banks owned, controlled, and operated by a state government. Currently, and to the surprise of many, there is one such institution in the United States—the Bank of North Dakota.¹

Recently, two bills directed toward the establishment of a state-owned “public bank” were considered by the Banking Committee of the New York State Assembly.² Among other things, this proposed institution would perform the following functions: (1) depository for public monies, (2) underwriter of obligations of state and political subdivisions, (3) lender primarily on an intrastate basis, and (4) provider of a “yardstick” by which the performance of conventional banking institutions could

¹Furthermore, public attention has most recently been directed to the general issue of state involvement in banking in light of the problems experienced by the Farmers Bank of the State of Delaware, 49.3 percent of its stock being owned by the State of Delaware.

²Assembly Bills 6531 and 6532, 1975.

*Read last page
for refs*

be measured. Similar legislation is pending in the Canadian province of British Columbia, and two California State Senators have recently requested that a feasibility study be made concerning the establishment of a state-owned bank in California.

Rationale behind state involvement in banking

State involvement in and ownership of banking institutions in the United States dates back to the late 1700s, varying between the extremes of minimal involvement to complete ownership and operation prior to the Civil War. However, almost all states—even though they did not actively participate in banking—either reserved the right to or were required by the state constitution or statutes to subscribe to a portion of the stock in newly organized banks.³ Motives for state involvement in banking were numerous, but major reasons included: (6)

- Profits. Since banks were a source of considerable profits, it was believed that profits derived from state participation in banking activities could eliminate, or at least reduce, the burden of state taxes.

- "Favored borrower." By owning and operating banks, the state assumed it would be able to borrow on better terms than elsewhere.

- Public depositories. Many state-owned banks were to function as depositories of state funds and to act as fiscal agents for the states.

- Public confidence. Due to widespread public concern and distrust of banks during this period, state ownership was thought to be a means of preventing the establishment of privately owned banks whose policies might be antithetical to the public interest.

³D.R. Dewey, *State Banking Before the Civil War* (Washington: United States Government Printing Office, 1910), p. 33.

- Provider of capital. Particularly in the southern and western regions of the country, the lack of private capital with which to finance agricultural and industrial development provided an impetus for state ownership of banks as a means of providing the needed capital. Several banks were established for the purpose of lending to agriculture and promoting internal improvement projects (e.g., canal and railroad development) within the states.

- "Relief institutions." A number of state-owned banks were established to ensure that credit would be extended to those persons who were unable to obtain it elsewhere, with the particular mission of providing relief to debtors.

Results of early state ventures into banking

By the end of the Civil War most of the states had removed themselves from active participation in banking. (See box for a capsule history of many of the state-owned banks.) In general, history reveals that state ventures into banking proved to be a costly experiment. While results varied from state to state, some general insights can be derived from the historical experience. Although state ownership was not the main cause of the failure (or success) of these institutions, the most conspicuous examples of failure occurred when the state had a free hand in the bank's affairs. In many instances the bank was controlled by incompetent political appointees who were subject to special interest group pressures and who used the bank to grant or deny political favors. These political appointees frequently had little regard for basic and sound banking principles.

At the outset both the state legislature and taxpayers approved of the state becoming a banker since they foresaw the profits arising from such a venture as a step toward achieving a taxless society.

Upon formation, however, the objectives of various special interest groups began to conflict. On the one hand, the state and taxpayers had a desire and a goal to make the bank profitable. In so doing, bank profits would provide needed state revenues and lessen tax burdens. On the other hand, the state and the bank's debtors wanted to use the bank to achieve "higher social goals," such as providing relief, developing resources, promoting internal improvements, etc. As a result, the "higher social goals" meant that the state-owned bank was to be sacrificed to its debtors. As soon as an economic or political crisis was at hand, "relief" was called for, which meant that the bank's debtors were to be relieved of their obligations to the bank. In the case of many of the state-owned banks, failure resulted when the state simultaneously attempted to live off the bank and plunder it.⁴

In light of numerous examples of state-owned bank failures and few examples of successes, it is instructive to examine the background and results achieved by the one remaining state-owned bank in the United States—the Bank of North Dakota.

The Bank of North Dakota

From 1915 to 1920, brought on largely by the pressures of World War I, the demand for agricultural products and industrial goods increased. Since agriculture was becoming increasingly mechanized, farmers required more credit to purchase machinery and to buy and improve land. In the western states a scarcity of deposits made it difficult for private banks to extend sufficient credit to meet the demands of agriculture. Although rural banks were, on average, heavy borrowers from the city banks, there was a growing outcry that the

⁴William Graham Sumner, *A History of Banking in the United States*, vol. 1: *A History of Banking in All the Leading Nations* (New York: The Journal of Commerce and Commercial Bulletin, 1896), p. 315.

city banks were draining money from the rural areas.⁵ Economic instability and unmet credit demands fostered demands for political action to remedy the situation.

Due to the scarcity of credit in North Dakota, farmers in the state became deeply indebted to the banks in Minneapolis, which—they argued—were charging inordinately high interest rates on both short- and long-term loans; even at these high rates the farmers could not be assured of securing credit. Lacking faith in the ability of the market system to allocate sufficient credit to agriculture, the Non-Partisan League committed itself to organizing a state-owned bank in North Dakota to be the "people's bank," both in terms of ownership and service.⁶

Proponents of the bank believed that it would retain funds locally and would extend credit to farmers on real estate mortgages. Also a "banker's bank," it would furnish credit and provide clearing services, thus making local banks less dependent upon banks in Minneapolis and other urban centers.

Early in 1919 the North Dakota legislature authorized the incorporation of the Bank of North Dakota, intending it to be an institution to promote economic development within the state, as was clearly stated in the Bank of North Dakota Act:

For the purpose of encouraging and promoting agriculture, commerce and industry, the State of North Dakota shall engage in the business of banking, and for that purpose shall, and does

⁵Charles S. Popple, *Development of Two Bank Groups in the Central Northwest* (Cambridge, Massachusetts: Harvard University Press, 1944), p. 73.

⁶Almost 100 years earlier (1820) the State of Kentucky had formed the state-owned Bank of the Commonwealth of Kentucky (popularly known as the "Peoples Bank"). Relief objectives, corrupt management, and currency depreciation forced the Bank of the Commonwealth of Kentucky to cease its lending activities ten years later.

Illinois

The Illinois Constitution of 1818 specified that there should be no banks in the state except a state bank and its branches. In response to widespread financial distress, and over the objections of the Governor of Illinois, the State Bank of Illinois—"an institution for relief of individual distress" and founded wholly on the credit of the state—was established in 1821. The bank's head office was at Vandalia, then the state capital, with branches in four other cities. The legislature exercised complete control over the bank's operations and elected the president and six directors of the head office. The bank was the sole depository of state funds.

From the beginning the bank's operations proved to be a serious burden on state finances. Problems arose primarily from two factors—inept management by political appointees and the liberal attitude which the state took toward the bank's debtors. The bank's charter expired in 1831 at which time the state was forced to borrow \$100,000 to wind up the bank's affairs. Total monetary loss to the state was estimated to be \$400,000; however, this does not reflect the loss incurred by private individuals nor the damage to the state's credit standing.

Alabama

The Alabama Constitution of 1819 specified the establishment of one state bank with branches. In 1823 the Bank of the State of Alabama was chartered "to provide for the safe and profitable investment" of public funds, an objective it failed to achieve. The state was the sole stockholder, and the General Assembly elected the president and twelve directors. The bank's charter expired in 1845, its history clouded by loan losses and political scandal. In 1867 the state constitution was amended to prohibit the state from being a stockholder in any bank.

Georgia

Under pressure from agricultural interests the State of Georgia in 1828 established the Central Bank of Georgia for the purpose of "making loans upon terms more advantageous than has heretofore been customary." The Governor chose the directors, and the bank

acted as the state's fiscal agent. Financial loss preceded the bank's closing, its affairs not being terminated until about 1856.

Indiana

The Indiana Constitution of 1816 was unique in the sense that it was the first state constitution to explicitly prohibit the establishment of banks, with the exception of a state bank with branches. In 1834 the State Bank of Indiana was incorporated for a period of 25 years. In part, the bank was organized to "encourage the development of the agricultural resources of the state" and to act as the state's fiscal agent. It was a tightly knit federation of banks under the general supervision of a Central Board at Indianapolis. The state held 50 percent of the stock, elected the president and four of the seven directors of the main bank at Indianapolis, and shared in the appointment of each branch was managed by local shareholders. Local control, mutual liability, and stringent supervision by the Central Board—not characteristic of other state-owned banks—proved to be key factors in the success of the bank, along with its existence as a pure monopoly within the state. The bank weathered the Panic of 1837, and when it wound up operations in 1857, it had paid regular dividends with the state realizing a net profit of about \$3.5 million. Constructive achievement displayed by the State Bank of Indiana served as an example that other states followed.

Arkansas

In 1836 Arkansas, following the example set by South Carolina, incorporated the Bank of the State of Arkansas. The president and twelve of the directors were appointed by the state legislature. The bank acted as the depository for state funds and was required to loan these funds throughout the state. Due to a combination of economic, political, and bank management factors, it was closed in 1842 and the State of Arkansas was left with a \$5 million debt as a reminder of its banking experience. The Arkansas Constitution was amended in 1846 to prohibit any banking institution from being established in the state.

hereby, establish a system of banking owned, controlled and operated by it, under the name of the Bank of North Dakota.

The bank was to have a capital stock of \$2 million to be subscribed for entirely by the state. In its early years instances of mismanagement, involvement in foreclosures on real estate loans, and political manipulation of the bank's affairs weakened public confidence in the institution. By 1924 the bank's operating losses were estimated at about \$1.8 million.⁷ Some confidence in the bank was regained during the 1930s when it supported the market for local government obligations.

From this rather dismal beginning the Bank of North Dakota has evolved into the largest commercial bank in the state. As of year-end 1975 its total deposits amounted to approximately \$311.7 million, representing about 11.9 percent of the state's total commercial bank deposits. The bank's aggregate net operating earnings over its 56-year history had amounted to approximately \$90.9 million.

From its inception the bank did not enter into direct competition with other commercial banks within North Dakota. Today it operates largely as a trust fund for public deposits and as a clearing house for many state institutions. The bank receives all of the deposits of the state agencies—as well as about 30 percent of the deposits of political subdivisions other than the state—and a limited amount of demand and time deposits from individuals. It also acts as a correspondent bank for many small unit banks within the state. All of the bank's deposits are state guaranteed.

Law prohibits the bank from making private and commercial loans, except Veterans Administration (VA) and Federal Housing Administration (FHA)

⁷Warren M. Persons, *Government Experimentation in Business* (New York: John Wiley and Sons, Inc., 1934), p. 188.

guaranteed home loans and federally insured student loans. These loans, as of year-end 1975, represented about 53 percent of the bank's total loans, which amounted to \$119 million. With total deposits of \$311.7 million the bank's loan-to-deposit ratio is about 38 percent, somewhat lower than the loan-to-deposit ratio for private commercial banks in the state. This low ratio is explained in part by the nature of the bank's public deposits and its commitment to the safety of public deposits.

The bank derives approximately 38 percent of its total operating income, which amounted to about \$25.4 million in 1975, from interest on loans. Interest expenses accounted for about 91 percent of the bank's total operating expense, which was \$17 million at year-end 1975. The ratio of total operating expense to total operating income in 1975 was 66.6 percent, which is above average compared to private commercial banks of similar size.

Commencing during the 1940s the bank became an active underwriter for bond issues of the state's political subdivisions. The bank has been criticized for its policy of holding tax-exempt securities since it pays no income tax. However, the management contends that the policy is both efficient and economically sound since many of the issues are so small as to preclude public bidding.

The question of whether the Bank of North Dakota has been an effective institution for fostering economic development within the state remains to be answered. On the surface it appears that the extent of development fostered by the bank is less than proportional to its size. Concern over the safety of its public deposits and the need to remain highly liquid has caused the bank to hold a large portion of its earning assets in a low risk, low return form. The trade-off between low risk and high return tends to hamper developmental potential.

Although the Bank of North Dakota was established, in part, to make agricultural loans available on a reasonable basis, it makes no direct farm loans; presently, its major contribution in supplying farm credit lies in the purchase of federally insured Farmers Home Administration (FmHA) loans and participations in agricultural loans made by other banks. To a certain extent the objectives of the bank were supplanted by the establishment of federal agricultural lending institutions and regulations which have expanded the alternative sources of agricultural credit.

State-owned banks: pitfalls and advantages

The history of state-owned banks reveals that in almost all cases the banks were established with the belief that existing financial institutions were not adequately meeting the financial needs of the state and/or the public. To fill the void, the states became bankers. With some notable exceptions their existence was short-lived; and, more often than not, they did not achieve their desired objectives.

On at least two recent occasions the Bank of North Dakota has been cited as a "valid historic precedent" which "proves that a state government can efficiently and effectively manage a banking institution." On the other hand, one might well cite the record of the Bank of the State of Arkansas or the State Bank of Illinois as establishing a "valid historic precedent." States considering the establishment of state-owned banks should be aware of both the pitfalls and the advantages that may be derived from bank ownership, as discussed below.

Proponents of state-owned banks assume that the state will be the recipient of profits (if any) currently being derived from public funds held by private financial

institutions. As such, it is contended that the profits derived from the state-owned banks will make the institutions self-supporting and will create no additional costs for the state. Carried one step further, profits derived from bank ownership will serve to lessen the overall state tax burden on the general public. Opponents, however, contend this line of reasoning is fallacious in at least two respects. First, an accounting must be made for the opportunity cost of funds employed. That is, the state must weigh the rate of return on investing scarce state resources (monetary as well as nonmonetary) in a state-owned bank against the rate of return these resources would yield in all other possible endeavors, both public and private. Second, opponents contend no empirical evidence supports the assumption that a profitable state-owned bank would necessarily cause a reduction in state tax burdens. For example, North Dakota's tax receipts per \$1,000 of personal income are about 9 percent above the national average. Although not sufficient grounds upon which to reject, neither is it sufficient grounds upon which to accept the hypothesis that the establishment of state-owned banks will ensure a reduction in state tax burdens.

Proponents also contend that the establishment of a state-owned bank would allow the state to pool its financial resources so as to achieve economies of scale and efficiencies with respect to their allocation and earning potential. Opponents insist that the benefits derived from pooled resources may be less than the costs involved. Also, evidence indicates that economies of large scale are slight once a bank approaches the \$10 million deposit size and are exhausted beyond the \$50 million deposit level. By concentrating the majority of its financial resources in one institution, the state will forego the safety that arises out of the distribution of public funds among numerous financial

intermediaries.⁸ Pooling of deposits increases a state's financial risk exposure⁹ and reduces its financial flexibility by preventing it from obtaining the highest possible yield on invested funds consistent with reasonable safety of principal. Furthermore, any financial institution which relies heavily upon state and local funds will experience large fluctuations in deposits due to the seasonal nature of state revenues and expenditures. Private commercial banks are able to compensate for these seasonal trends by diversifying their deposit base. Lacking a similarly diversified base, state-owned banks will be constrained in achieving their next major goal, that of allocating credit toward "socially desirable investments."

In addition, proponents claim that public funds placed in private financial institutions are loaned out for both interstate and intrastate, as well as international purposes. By centralizing its financial resources in a state-owned bank, a state has the ability to extend credit on an *intrastate* basis and can channel this credit toward certain "socially desirable investments" in order to combat unemployment, credit discrimination, and other social problems. Opponents argue that the history of state-owned banks indicates such an institution, over the long run, would be unable to maintain, as a major objective, the allocation of credit to "socially desirable investments." Furthermore, once the state assumes the role of banker, it will be faced with the problems confronting private commercial banks, such as controlling risk exposure, maximizing returns

⁸A case in point is the Farmers Bank of the State of Delaware, the sole depository for state funds. Loan losses of about \$17 million in 1975 necessitated actions on the part of the state and the FDIC to protect \$140 million in state funds on deposit with the bank.

⁹Delaware's "high exposure" to risk due to its more than \$100 million of uninsured deposits in the Farmers Bank has been cited as a contributing factor in the recent lowering of the rating of the state's general obligation bonds to single-A from single-A-1.

on investments, and ensuring adequate liquidity and capital. The process of channeling its resources primarily toward "socially desirable investments" will at the very least necessitate a trade-off between risk and return. A major problem to be resolved will be the identification of socially desirable investments. Assuming that investments can be agreed upon to the mutual satisfaction of all parties involved, the transaction costs (for example, the need for elaborate and time-consuming studies to determine demand functions without being able to observe a market) must be weighed against the hoped-for increase in public benefits arising out of the nonmarket solution for the allocation of resources.

Last, but not least, proponents contend that the state-owned banks will serve as a "yardstick" by which the performance of private commercial banks can be measured. Opponents maintain such institutions would be encumbered with political administration, would be tax exempt, and would be generally insulated from the rigors of competition from other financial institutions; thus they would be of little or no value as "yardsticks."

In the final analysis the decision concerning the establishment of a state-owned bank must be made on the basis of the social costs and benefits anticipated for such an institution. Only if there are net public benefits to be derived from such an institution should the states seriously consider employing scarce financial resources. In making their decision the states might well consider Samuel Clemens's remark concerning the cat who inadvertently sat on a hot stove lid: "She will never again sit down on a hot stove lid; but also she will never sit down on a cold stove any more." Clemens concluded, "We would be careful to get out of an experience only the wisdom that is in it—and stop there."

David R. Allardice

AUDIT DIVISION
SB 171

In the 61 audit reports the Audit Division presented to the Legislative Commission in the last two years, there were many recommendations regarding the creation and repeal of "funds" in the State's Accounting System. Most of the funds created in this BDR were already in existence, having been created administratively. The funds being abolished were not being used and the accounting was being accomplished in some other fund.

The following agencies are affected:

	Sections
Attorney General	1,51,55,61
Department of General Services	2,10,11,14,15,16,17,18,19, 20
Budget Office	3,21
Department of Commerce	4,33,52,53,54,56,57,58,59, 60
Parole and Probation	5,6,7
Governor's Office	8,61
Department of Conservation and Natural Resources	9,24,25,26,29,34,35,36,37, 38,39,40,41,42,43,44,45,46, 47,48
Treasurer's Office	12,13,23,61
Legislature	22
Department of Motor Vehicles	27,30,31,32
Racing Commission	28
Agriculture	49,50
Administratively created funds legalized	11
One new fund created (Forestry)	<u>1</u>
Total funds put in law	<u><u>12</u></u>
Number of funds removed from statutes, however function for which fund was put in law not changed	<u>9</u>
Number of funds transferred from one agency to another (Revenue Sharing Trust Fund)	<u>1</u>
Number of funds only categorized as to type	<u><u>20</u></u>

During the 1977 Session, AB 67 was enacted which provided for the identification of funds by fund types. Accordingly, NRS 353.321 reads:

"1. The state controller shall report each fund and group of accounts in one of the following categories for annual financial statement purposes:

- (a) State general fund;
- (b) Special revenue funds;
- (c) Capital projects construction funds;
- (d) Intragovernmental service funds;
- (e) Enterprise funds;
- (f) Trust and agency funds;
- (g) Debt service funds;
- (h) General long term debt group of accounts; or
- (i) General fixed assets group of accounts.

2. All resources and financial transactions of the state government shall be accounted for within a fund or group of accounts. The state controller shall assign each existing fund and group of accounts which is created by statute to the proper category unless the category is designated by statute."

While in this bill we have created 12 funds and abolished 9, we also have identified several funds as to category.

ATTORNEY GENERAL

(Sections 1,51,55,61)

Section 1 creates the Attorney General's Special Fund. This fund is already being used in the Controller's System. In that fund is also being accounted the Unfair Trade Practices Fund (Section 51), and the Private Investigator's Fund (Sections 55 and 61). Accordingly, the later two funds are not necessary and while we have not eliminated the functions, we have provided for the proper accounting within the existing system.

THE DEPARTMENT OF GENERAL SERVICES

(Sections 2,10,11,14,15,16,17,18,19,20)

We have only created two funds - One in the Director's Office (Section 2), and one in Purchasing. The rest of the sections identify the funds as intragovernmental service funds. The purpose is to clearly establish the fact these are to operate as a business. They are to charge for their services and include, among other things, a factor for depreciation of fixed assets in their billing rates.

REVENUE SHARING TRUST FUND
(Sections 3,61)

The Budget Office, not the Treasurer, should have responsibility for this fund. We also eliminate reference to the Governor handling Special Revenue Sharing money which authority terminated in 1973.

DEPARTMENT OF COMMERCE
(Sections 4,33,52,53,54,56,57,58,59,60)

We have created only one fund, that being in the Real Estate Division. Again this was already created administratively. The rest of the sections identify the funds as to category.

PAROLE AND PROBATION
(Sections 5,6,7)

We created one fund; the Restitution Trust Fund, and made accounts out of two loan funds.

GOVERNOR'S OFFICE - HIGHWAY SAFETY
(Section 8)

We identified the fund as to category.

CONSERVATION AND NATURAL RESOURCES
(Sections 9,24,25,26,29,34,35,36,37,38,39,40,41,42,43,44,45,
46,47,48)

Director's Office: We created an all inclusive trust fund, Section 9, and repealed another (Section 47).

In regard to Section 48 which repeals the annual audit requirement of the Soil Conservation Commission, they fall under the Legislative Auditor's authority.

Parks Division: Two funds are created, the most important one being in Section 25 where the Capital Projects Construction Funds are created. This is the same as a provision we have for the Public Works Board. Many capital projects are presently accounted for in the General Fund, which is wrong.

Forestry Division: Made an account out of a fund. More importantly, in Section 34, we created a fund to account for all of the nursery activities of the Division.

Water Resources: We repealed one fund (Section 36) and created one (Section 37).

TREASURER'S OFFICE
(Sections 12,13,23)

We identify one fund (Section 12), as to category and make an account out of a fund (Section 23).

DEPARTMENT OF MOTOR VEHICLES
(Sections 27,30,31,32)

We are creating 2 funds that already exist in the system (Sections 27 and 32). We are identifying one fund as to category (Section 30), and abolishing reference to a revolving fund (Section 31).

RACING COMMISSION
(Section 28)

We have identified fund by category.

AGRICULTURE
(Sections 49,50)

Change language to eliminate "Fund Account". Should only be Fund.

SB 171
REQUESTED AMENDMENTS
PAGE 4, LINES 14-23

4. Costs of preparation of the highway safety program [shall] must be paid from the highway safety program planning fund which is hereby created [in the state treasury. Such fund shall consist of moneys] as a special revenue fund. [The fund consists of money] Money provided by direct legislative appropriation must be accounted for in the fund and [by] money received from the Federal Government and by donations, which the agency may accept, must be deposited in the state treasury for credit to the fund. The state agency designated by the governor pursuant to subsection 2 [is authorized to] may make the necessary applications for federal [funds] money and provide required demonstrations that federal [moneys] money will be matched with state [funds] money in the highway safety program planning fund.

PAGE 11, LINES 31-37

Sec. 27. NRS 445.700 is hereby amended to read as follows:
445.700 1. In areas of the state where and [at such times as] when a program [of implementation] is commenced pursuant to NRS 445.630 to 445.670, inclusive, the following fees [shall] must be paid to the department of motor vehicles and [deposited in with the state treasury: treasurer for credit to] must be accounted for in the pollution control fund which is hereby created as a special revenue fund:

EXHIBIT 145

AMENDMENTS TO S.B. 171

Submitted by Milos Terzich, Esq., representing American Council of Life Insurance.

Amend Section 57, page 23, as follows:

I. Amend line 25, page 23, by adding, after the word staff, "without limitation as to number,"

II. Amend line 35, by adding new subsection 2:

"2. The expenses incurred under subsection (a) and (b) of Section 1 shall be paid without regard to the limitations expressed in N.R.S. 281.160 or in any state agency regulations."

III. Amend line 35, page 23, by inserting subsection 3 immediately preceding the word "All".

IV. Amend line 38, page 23, by deleting the word "paid" and inserting the word "processed".

V. Amend line 39, page 23, by deleting the word "paid" and inserting the word "processed".

ASSEMBLY BILL NO. 176—ASSEMBLYMAN HARMON

JANUARY 23, 1979

Referred to Committee on Government Affairs

SUMMARY—Removes requirement to mail certain county license regulations.
(BDR 20-610)

FISCAL NOTE: Effect on Local Government: No.
Effect on the State or on Industrial Insurance: No.

EXPLANATION—Matter in *italics* is new; matter in brackets [] is material to be omitted.

AN ACT relating to county government; removing requirement to mail certain county license regulations to licensees and attorneys in the county; providing for public inspection of those regulations; and providing other matters properly relating thereto.

The People of the State of Nevada, represented in Senate and Assembly, do enact as follows:

1 SECTION 1. NRS 244.345 is hereby amended to read as follows:
2 244.345 1. Every *natural* person, firm, association of persons or
3 corporation wishing to engage in the business of conducting a billiard
4 or pool hall, dancing hall, bowling alley, theater, softdrink establishment,
5 gambling game or device permitted by law, or other place of amusement,
6 entertainment or recreation, outside of an incorporated city or incorpor-
7 porated town, [shall:] *must*:
8 (a) Make application by petition to the license board [, as provided
9 in subsection 2,] of the county in which [any such] *the* business is to
10 be engaged in, for a county license of the kind desired. [Such application
11 shall] *The application must* be in a form prescribed by the regulations
12 of the license board.
13 (b) File the application with the required license fee with the county
14 license collector, who shall present the [same] *application* to the license
15 board at its next regular meeting.
16 The board may refer the petition to the sheriff, who shall report upon
17 [the same] *it* at the following regular meeting of the board. The board
18 shall [then and there] *at that meeting* grant or refuse the license prayed
19 for or enter [such] *any* other order [as is] consistent with its regula-
20 tions. Except in the case of an application for a license to conduct a
21 gambling game or device, the sheriff may, in his discretion, grant a
22 temporary permit to an applicant, valid only until the next regular meet-
23 ing of the board. In unincorporated towns and cities governed under the
24 provisions of chapter 269 of NRS, the license board [shall have] *has*

SENATE BILL NO. 171—COMMITTEE ON GOVERNMENT AFFAIRS

FEBRUARY 1, 1979

Referred to Committee on Government Affairs

SUMMARY—Revises designations of various accounts and funds. (BDR 31-256)

FISCAL NOTE: Effect on Local Government: No.
Effect on the State or on Industrial Insurance: No.

EXPLANATION—Matter in *italics* is new; matter in brackets [] is material to be omitted.

AN ACT relating to public finance; revising the designations of various accounts and funds; and providing other matters properly relating thereto.

The People of the State of Nevada, represented in Senate and Assembly, do enact as follows:

- 1 SECTION 1. Chapter 228 of NRS is hereby amended by adding
2 thereto a new section which shall read as follows:
3 1. *The attorney general's special fund is hereby created as a special*
4 *revenue fund.*
5 2. *Except as otherwise provided by NRS 598A.260, all money*
6 *received by the attorney general pursuant to those provisions of law relat-*
7 *ing to private investigators and to recoveries for unfair trade practices*
8 *must be deposited in the state treasury for credit to the attorney general's*
9 *special fund.*
10 3. *All claims against the fund must be paid as other claims against the*
11 *state are paid.*
12 SEC. 2. Chapter 232 of NRS is hereby amended by adding thereto a
13 new section which shall read as follows:
14 1. *The department of general services operating fund is hereby cre-*
15 *ated as an intragovernmental service fund.*
16 2. *The operating budget of each division of the department of gen-*
17 *eral services must include an amount representing that division's share of*
18 *the operating costs of the director's office and the central accounting func-*
19 *tion of the department. This amount must be transferred to the operating*
20 *fund from the appropriation made to that division from the state general*
21 *fund.*
22 3. *All money received by the director's office, including that received*
23 *for the central accounting services of the department, must be deposited in*
24 *the state treasury for credit to the operating fund.*

SENATE BILL NO. 197—SENATOR BLAKEMORE

FEBRUARY 8, 1979

Referred to Committee on Government Affairs

SUMMARY—Permits certain district attorneys who reside outside their respective counties same salary as those who reside within their respective counties. (BDR 20-1067)

FISCAL NOTE: Effect on Local Government: Yes.
Effect on the State or on Industrial Insurance: No.

EXPLANATION—Matter in *italics* is new; matter in brackets [] is material to be omitted.

AN ACT relating to county officers and employees; permitting a district attorney who resides outside the county he serves, but within a specified distance of the county line, to draw the same salary as if he were a resident of that county; and providing other matters properly relating thereto.

The People of the State of Nevada, represented in Senate and Assembly, do enact as follows:

- 1 SECTION 1. NRS 245.043 is hereby amended to read as follows:
- 2 245.043 1. As used in this section:
- 3 (a) "County" includes Carson City.
- 4 (b) "County commissioner" includes the mayor and supervisors of
- 5 Carson City.
- 6 2. Except as provided by any special law, the elected officers of the
- 7 counties of this state are entitled to receive annual salaries in the base
- 8 amounts specified in the following tables. The annual salaries are in full
- 9 payment for all services required by law to be performed by such officers.
- 10 Except as otherwise provided by law, all fees and commissions collected
- 11 by such officers in the performance of their duties shall be paid into the
- 12 county treasury each month without deduction of any nature.

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