

Continental Divide: The Canadian Banking and Currency Laws of 1871 in the Mirror of the United States

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In the wake of the 2008 financial crisis, international observers praised the stability of Canada's banks. When financial institutions in the United States and the United Kingdom collapsed, Canada did not experience any bank failures. The World Economic Forum's *Global Competitiveness Report* rated Canada's banking system as the most sound in the world.¹ Historically, bank failures have been quite rare in Canada. Some authors argue that the stabilizing features of Canada's financial system were established in the first five years after the creation of the Canadian nation-state in 1867.² This paper will examine the making of the Canadian banking law in 1871, an event widely regarded as a crucial turning point in Canadian financial history.

The 1871 banking law helped to set Canadian banks on a very different path from that of the United States. Economic and business historians frequently contrast Canada's banking sector with that of the United States.³ Whereas the United States had a large number of small banks, numerous bank failures, and many statutory restrictions on intrastate and interstate branching, a few large and stable firms with branches in every region of the country dominated Canadian banking. Canada had very few insolvencies after 1871

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doi: 10.1093/es/khr052

Advance Access publication January 19, 2012

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1. Rob Taylor, "Canada Rated World's Soundest Bank System: Survey," *Reuters News*, October 9, 2008.

2. The most recent author to do so is MacIntosh, "Origins of Financial Stability in Canada: The Bank Act of 1871," in *Relentless Change*, ed. Martin, 21–38.

3. Norrie et al., *A History of the Canadian Economy*, 180; Southworth, *Branch Banking*, 199; McIvor, *Canadian Monetary, Banking and Fiscal Development*, 12–64.

and in most cases, the depositors and noteholders were able to get their money back. At times shareholders were even able to recoup part of their investments.⁴ Data from the early twentieth century show that Canada's banks were also more profitable than those operating in the United States's more competitive environment.⁵ The Canadian system of transcontinental branch banking helped protect depositors by ensuring that the viability of a bank was not tied to the fate of any single community. The same could not be said of the unit (single-location) banks so common in the United States. Not all economic historians agree that branch banking would have made the US banking system more resilient.⁶ However, Charles Calomiris has argued persuasively that the most important single cause of financial instability in the United States was state and federal regulations restricting branching. Such restrictions inhibit diversification and make banks more vulnerable to economic downturns, which in turn helps to explain why US banking failures and panics were both more numerous and more severe than banking downturns in Canada, Australia, the United Kingdom and other countries that permitted branching.⁷ Another advantage of the Canadian system of nationwide branch banking was that it efficiently moved capital from savers to areas of recent settlement where capital was needed.⁸ In contrast to the United States, where the absence of interregional branch banking resulted in major regional disparities in borrowing costs, bank branches throughout Canada charged similar rates, except in the sparsely settled north-west territories.⁹

The banking laws of 1871 integrated the financial systems of the previously separate colonies and became crucial parts of the project of making the Canadian nation state.¹⁰ William Marr and Donald Paterson have summed up the scholarly conventional wisdom as follows: "The Bank Act of 1871 was also critical in establishing control over the banking system, both in itself and because it became the model for subsequent Bank Acts."¹¹ Technically, the "Bank Act of 1871" consisted

4. See table "Canadian Bank Insolvencies since 1867," in Glazebrook, "Finance and Banking," in *Cambridge History of the British Empire*, ed. Rose, 6:640; Neufeld, *The Financial System of Canada*, 97.

5. Bordo et al., "The U.S. Banking System from a Northern Exposure," 325–41; Nichols and Hendrickson, "Profit Differentials between Canadian and U.S. Commercial Banks," 674–96.

6. Carlson, "Are Branch Banks Better Survivors?"

7. Calomiris, *Bank Deregulation in Historical Perspective*, 3.

8. Frost, "The 'Nationalization' of the Bank of Nova Scotia, 1880–1910," 3–38.

9. Lash, *The Banking System of Canada*, 13–16.

10. Innis, ed., *An Economic History of Canada*, 216; Baskerville, *A Concise History of Business in Canada*, 378.

11. Marr and Paterson, *Canada: An Economic History*, 254.

of several pieces of legislation passed in 1870 and 1871.¹² This bundle of statutes laid the foundations for oligopoly, branch banking, and relative stability. By the 1890s, a few large corporations with branch networks extending from the Atlantic to the Pacific controlled Canadian banking. Their monetary and regulatory framework was informed by a Canadian financial orthodoxy that mandated oligopolistic banking, adherence to the gold standard, and interest charges set by market forces rather than by usury laws. Connected to these three principles was a vision of where Canada would obtain the capital needed to finance its development: Britain. Much of the Canadian political elite thought that Canada needed to align its financial laws with those of the mother country if the colony was to have access to British capital. The belief that British, rather than domestic or American savings, should remain the engine of growth in Canada was the fourth pillar of the young Dominion's financial orthodoxy.

Canadian bank failures were both less common and less catastrophic for the interested parties than bank failures in the United States. The strength of the Canadian financial system was demonstrated in the crises of 1873, 1893, and 1907, and during the Great Depression. Unlike the United States, Canada did not experience a banking panic in 1873, although several forced amalgamations and minor bank failures occurred later in that decade. In 1893, over six hundred US banks suspended operations, many forever. In contrast, just one Canadian financial institution, newly established in Manitoba, suspended repayment. Moreover, the bank soon resumed activities.¹³ After the 1983 financial crisis, an American, R. M. Breckenridge, wrote a report presenting Canadian banking as a model for the United States.¹⁴ Buoyed by such praise from outside, Canadian bankers congratulated themselves on their system's stability and efficiency.¹⁵

In a recent article in this journal, Professor Richard Sylla contrasted Canada's slow growth before 1840 with the rapid development of the contemporary United States and then attributed Canada's retardation to primitive financial institutions. He wrote: "Canadian political economy did not permit a financial revolution to occur. US political

12. These pieces of legislation were: "An Act to Establish One Uniform Currency for the Dominion of Canada," 34 Victoria (1871), chap. 4; "An Act Relating to Banks and Banking," *ibid.*, chap. 5; "An Act Respecting Certain Savings Banks in the Provinces of Ontario and Quebec," *ibid.*, chap. 7.

13. Lash, *The Banking System of Canada*, 13–16.

14. Breckenridge, *The Canadian Banking System, 1817-1890*. This book was reissued in 1910 by the US National Monetary Commission. See "Banking in Canada," *New York Tribune*, January 29, 1910, 4.

15. For an example of this type of self-congratulatory discourse, see Walker, *A History of Banking in Canada*. Walker was later president of the Canadian Bank of Commerce.

economy did.” Unfortunately, Professor Sylla did not extend his analysis to the period after 1867, when Canada laid the legal foundations for what is arguably the most reliable banking system in North America.¹⁶ This essay will fill the gap in the existing literature by examining the politics of banking in the half decade after the creation of the Canadian federal state, and it will also show that the distinctive features of post-1871 Canadian banking owed much to the fact that British North America was part of the British Empire rather than an independent republic. Existing works in Canadian banking history, most notably Bray Hammond’s chapter on Canada in his study of antebellum North American banking, largely ignore the imperial dimension. Hammond endorsed historian Adam Shortt’s argument that the distinctive features of the Canadian banking system were inspired by Alexander Hamilton.¹⁷ He observed that “though the handiwork of Alexander Hamilton practically disappeared from American banking, it survives still in the Dominion.” Hammond also noted that Hamilton’s plans for American banking were based on the study of the Bank of England Act of 1694: “Banking in British North America, therefore, came from a British source by way of the United States and its first Treasury head.”¹⁸

Hammond was right to emphasize the Hamiltonian roots of Canada’s banking system: many of the earliest Canadian bank charters recycled entire paragraphs from charters and articles of association Hamilton drafted for American banks.¹⁹ Moreover, the attitudes and values of Canadian policymakers in the 1860s bear a striking resemblance to those of Hamilton and the other Federalists of the 1790s. However, there are some crucial differences between nineteenth-century Canada’s banking laws and the system Hamilton outlined for the US. Hamilton expressed skepticism about the wisdom of having a “plurality of branches” in his 1790 *Report on a National Bank*,²⁰ leading Hammond to conclude that he was categorically opposed to branching.²¹ However, David J. Cowen’s archival research has shown that Hamilton later came to support the establishment of branches of the Bank of the United States. Indeed, he even lobbied for one in Virginia.²² Still, the versions of Hamilton’s *Report* republished in 1810,

16. Sylla, “Political Economy of Financial Development,” 665.

17. Shortt, “Early History of Canadian Banking,” 19.

18. Hammond, *Banks and Politics*, 662.

19. *Ibid*; 646.

20. Alexander Hamilton, “Report on a National Bank, Dated Treasury Department, December 13, 1790,” in *Reports of the Secretary of the Treasury of the United States*, 69.

21. Hammond, *Banks and Politics*, 126.

22. Cowen, *Origins and Economic Impact*, 56.

1811, 1831, 1837, and 1908 contained the admonitions against branch banking, which doubtless influenced contemporary thinking more than the pro-branching sentiments expressed in some of Hamilton's unpublished correspondence.²³ Nineteenth- and twentieth-century Americans of various persuasions remained suspicious of branches, meeting most of their banking needs through unit banks.

In contrast, transcontinental branch networks became a feature of Canadian banking, echoing transatlantic patterns. Although England's banks were only beginning to build extensive branch networks in this period, other jurisdictions within the British Empire had developed branch banking by the 1860s. It emerged in Scotland in the eighteenth century and was legalized in England and Wales in 1826. At first, English bankers were slow to take advantage of the new laws and the growing ease of travel to create branch networks. However, the decisive shift away from unit banking and toward branching in England started in the 1860s.²⁴ Britain also developed its so-called imperial banks, which had branches in multiple colonies, including some that became part of the Canadian federation. In studying this period of Canadian history, one is struck by the sheer anglophilia of Canada's elite, who sought knighthoods and closely identified themselves with all things British. This anglophilia also influenced the country's banking laws. Remarkably, during the 1870–1871 debate on banking in the Canadian parliament, all the participants took the existence of branches essentially for granted: the debate focused on other aspects of the proposed law. One cannot understand why there was a consensus in favor of branch banking without taking the influence of Britain into account.

Moreover, the British influence on Canadian political culture affected the evolution of the country's banking system indirectly. Even today, the Canadian version of democracy involves voters' greater degree of deference to elected politicians than would be normal in the United States. The predominant theory of parliamentary representation in Canada has been the "trustee principle," which says that legislators must advance their constituents' interests, not their wishes. This interpretation of democracy is very different from the popular American theory that congressmen ought to act as delegates for their constituents.²⁵ Had they been put to the Canadian electorate in a referendum, the basic principles of the Canadian banking and currency statutes of 1870 and 1871 (i.e., the gold standard, regulations that promoted oligopolistic banking, laws favoring creditors over

23. Republication dates taken from the Library of Congress catalogue.

24. Newton and Cottrell, "Joint Stock Banking," 127; Munn, "Banking on Branches."

25. Franks, *The Parliament of Canada*, 57.

debtors) would likely have failed by a landslide. Under such a scenario, Canada might have acquired a decentralized banking system similar to that of the United States. Instead, Canada's banking and currency laws reflected the ideas of a small elite of political and business leaders rather than those of the uneducated masses. Hence the semi-democratic nature of Canada's political system, rather than differences between Canadian and American values, shaped Canada's banking and currency laws after 1867.²⁶

The Canadian constitution of 1867 blends features of the British and American constitutions. Canada's elites believed in a system that blended monarchy and aristocracy with democracy, which is why the 1867 constitution provided for an unelected upper house inspired by the British House of Lords.²⁷ Moreover, Canada's political institutions and culture were, in 1870, substantially less democratic than those of the United States, although Canada had advanced closer to universal suffrage than had the United Kingdom.²⁸ Politicians in Canada admired the British political system and still regarded "democracy" as an American, and therefore suspect, concept. In the northern United States, nearly every White man had the right to vote, but a variety of property qualifications restricted the franchise in Canada. In the early nineteenth century, when land in British North America had been abundant, the property qualifications had resulted in something close to universal manhood suffrage, at least for Whites. However, as historian John Garner reports, the increasing scarcity of land in Canada had the effect of restricting access to the franchise. In the late 1850s, the legislature actually increased the property qualifications for voting, which contributed to a 24 percent *drop* in the number of voters in Lower Canada. In the 1860s, most British North American politicians except those of the quasi-republican *parti rouge* opposed manhood suffrage. In 1865, a newspaper located close to the American border denounced the corruption of our "Yankee neighbors," due to "universal suffrage and dollar worship."²⁹ During

26. There is a sizeable body of historical and sociological literature on why Canada developed different approaches than the United States to such issues as health care, gun control, and capital punishment. One group of scholars emphasizes differences in the values of voters in explaining why the two countries have different policies. Others argue that the difference in policy outcomes is mainly shaped by the ways in which the two political systems process the values inputted by their respective electorates. A thorough and up-to-date introduction to this literature is provided in Kaufman, *The Origins of Canadian and American Political Differences*.

27. Winks, *Canada and the United States*, 15–23.

28. Boyer, *The People's Mandate*, 19.

29. Garner, *The Franchise and Politics in British North America, 1755–1867*, 115. The quotation is from the *St. Catherines Evening Journal*, February 22, 1865, cited in Garner, *The Franchise and Politics*, 7.

the American Civil War, many Canadians sympathized with the South on the grounds that it was more “aristocratic” than the North.³⁰ As the historian David Cannadine shows, the most ambitious Canadian politicians sought knighthoods and invitations to stay in the country houses of British aristocrats. Indeed, British monarchs eventually appointed a few of their Canadian subjects to the House of Lords.³¹ Skepticism about the benefits of unalloyed democracy persists in Canada to this day. Canada’s political class continues to frown upon such American practices as elections for judges or the frequent use of referenda.

Canada’s political leaders in the 1860s were also inclined toward a relatively centralized political system. The Civil War in the United States had discredited federalism in the minds of many Canadians. When John Scoble told his colleagues in the Canadian parliament in 1864 that the American Civil War proved that federal as opposed to legislative unions did not work, he was summarizing the conventional wisdom.³² The designers of the Canadian constitution admired the UK’s unitary state with just one elected legislature, the House of Commons at Westminster. The constitutional delegates of 1864 wished to replicate British political institutions “so far as our circumstances will permit.”³³ Some English-speaking delegates wanted to create a unitary state, but the need to accommodate autonomy-seeking French Canadians resulted in a constitution that blended American decentralization and the British unitary state.³⁴ In an 1865 book on federal government, Canadian politician Thomas D’Arcy McGee remarked that the people of Canada, “like all other American communities (when compared with European countries) have necessarily very decided democratic tendencies within them.” The task of Canada’s leaders was to resist this tendency by seeing that “authority is exalted” through strengthening the central executive power in any future Canadian federation. McGee regarded “executive impotency” as the major cause of the social disorder that was, in his eyes, an inevitable outcome of any federal system. Although he conceded that the US constitution of 1789 was “a vast advance on the previous Articles of Confederation,” it nevertheless provided far too weak a government due to the compromises nationalist statesmen

30. Winks, *Canada and the United States*, 22–23, 77.

31. Cannadine, *Ornamentalism*, 27–40.

32. Careless, *Brown of the Globe*, vol. 2, 120.

33. “Quebec Resolutions” in *Confederation: Being a Series of Hitherto Unpublished Documents*, ed. Pope, 38–52.

34. Letter from J. A. Macdonald to M. Cameron, 19 December 1864, quoted in Martin, “Archival Evidence and John A. Macdonald Biography,” 91.

such as Alexander Hamilton had been forced to make with “state jealousy” and the “wild theories of the demagogues of the day,” by which he probably meant Thomas Jefferson and the Anti-Federalists.³⁵

The hostility of Canada’s political class to democracy had a major bearing on the banking laws and also influenced the very process that created the Canadian federation. The ratification of the United States constitution in the 1780s had involved constitutional conventions elected by voters in each state. When New York’s politicians drafted a new state constitution in 1868, they put it to the people with a referendum, an even more democratic process.³⁶ In contrast, the approval of Canada’s new constitution in the 1860s involved quick votes in the legislatures of the several provinces and then the passage of an enabling statute by the British parliament.³⁷ When a few radicals in Canada had the temerity to demand a referendum on the subject, newspapers connected to the two main political parties denounced their presumption.³⁸

Still, Canadian political culture in the 1860s did resemble American political culture in the 1790s. It should be remembered that the United States was substantially more democratic in the mid-nineteenth century than it had been in the 1790s, when the Federalist Party dominated national politics. The presidencies of Thomas Jefferson and Andrew Jackson witnessed the accelerated democratization of American politics. Most states extended the right to vote to all adult White males, even those who lacked property. The expectation that the common people would defer to the social elite, standard in the Federalist Era, had been discarded. Elections also became more competitive and more frequent. The result was a political system that was much more responsive to public opinion. According to historian Gordon S. Wood, the “once derogatory terms of ‘democrat’ and ‘democracy’ [turned] into emblems of pride” for Americans. These trends horrified Alexander Hamilton and other Federalists, who associated democracy with social leveling and anarchy. For their part, the Democrats labeled their opponents as elitists, anglophiles, and crypto-monarchists.³⁹ The advent of

35. McGee, *Notes on Federal Governments*, 51, 52, 44, 34.

36. Dougherty, *Constitutional History of the State of New York*, 223. The ratification of the new Australia constitution in 1900 was also put to the people in a referendum. Irving, “Sister Colonies,” in *Shaping Nations*, ed. Cardinal and Headon, 27–38.

37. Hodgins, “Democracy and the Ontario Fathers of Confederation,” in *Profiles of a Province: Studies in the History of Ontario*, ed., Firth, 83–91; Wise, “The Annexation Movement and Its Effect on Canadian Opinion, 1837–67,” in *Canada Views the United States: Nineteenth Century Political Attitudes*, ed. Wise and Brown.

38. As quoted in Waite, *The Life and Times of Confederation*, 122.

39. Wood, *Empire of Liberty*, 16–17, 302–3, 312, 712–21, quote from 718.

Jacksonian Democracy in the 1820 and 1830s moved the United States still further from the social model the Federalists envisioned. These shifts in American political culture impacted US banking laws. Hammond showed the Jacksonians' desire to destroy the Second Bank of the United States, the country's de facto central bank, derived from their suspicion of monopolies and British-style financial institutions, views deeply lodged in republican ideology.⁴⁰

A similar trend toward a more democratic form of politics was at work north of the border, but it was far less pronounced. In the 1840s and 1850s, Canadian politics was transformed by the advent of "Responsible Government," which saw the introduction of a British-style system of prime ministers and party government into the colonies. Henceforth, real power would lie with a prime minister indirectly elected by the colonists, not with British-appointed governors. The emergence of a somewhat less deferential style of politics and the rise of the press and civil society institutions such as debating societies accompanied the advent of home rule within the Empire.⁴¹ Nevertheless, Canadian political culture remained much less democratic than that of the United States. Indeed, the creators of the Canadian constitution in the 1860s frequently expressed their admiration for Alexander Hamilton and his project of creating a centralized nation-state. They anticipated a strong and active federal government with unlimited authority over matters of economic policy.⁴² Scholar Gordon T. Stewart observed that compared to British and American politics in this period, "Canada's constitution and political culture was emphatically . . . statist in orientation."⁴³

Recent research on the comparative history of North American banking has underscored the importance of social class and race. Using data from the early twentieth century, Raghuram G. Rajan and Rodney Ramcharan found that the US counties in which land ownership was highly concentrated or a large proportion of the population was Black had less-developed banking institutions than the counties in which most people were White and wealth was more evenly distributed. They suggested that the landed elite of the Southern states (i.e., descendants of antebellum plantation owners) used the political process to restrict the growth of financial institutions that might have undercut their power as local creditors.⁴⁴ These

40. Hammond, *Banks and Politics*, 326–9, 378–81.

41. Keith, *Responsible Government*; McNairn, *Capacity to Judge*, 43–7, 240–3, 246–52.

42. Smith, "Toryism."

43. Stewart, *Origins of Canadian Politics*, 58.

44. Raghuram G. Rajan and Rodney Ramcharan, Table 2, in "Landed Interests and Financial Underdevelopment."

distinctly Southern social conditions discussed were very different from those in the Northern States and the adjoining regions of Canada, where freehold farms worked by White families, not plantations, were the foundation of society.⁴⁵ Canada did not have a “landed elite” in any meaningful sense of the term, since French Canada’s seigneurial system, a modified form of feudalism, had been abolished in the 1850s.⁴⁶

However, Rajan and Ramcharan’s research is useful because it illustrates the importance of legislative capture in the design of financial regulations. Evidence for regulatory capture is clear when we look at the legislative history of banking in Canada: leading politicians, including Canada’s first Minister of Finance and first prime minister, had very close ties to the major banks. Whereas the struggle over banking legislation in the Southern States pitted landed elites against proponents of banking expansion, the political dynamic in Canada involved a contest among different groups of bankers and other nonlanded elites. In the background of this struggle were agrarian politicians who depicted themselves as opponents of financial monopoly and champions of the common man. The politics of banking in Canada in the 1860s were similar to the late nineteenth-century struggle over branch banking in the United States. As Eugene Nelson White has shown, efforts by big city bankers to repeal the laws against branch banking were frustrated by a more powerful coalition of small country banks, which mobilized its political clout in both Washington and the state capitals to preserve unit banking in most states well into the twentieth century. Associations of unit banks such as California’s League of Independent Bankers used terms such as “democracy,” “autocracy,” and “decentralization” in their appeals to the public. The unit bankers’ invocation of Populist rhetoric appears to have been successful because state legislators approved bans on branching in many western, midwestern, and southern states, and, in one case, voters did the same in a referendum.⁴⁷

Political Background

Prior to 1867, Canada as we know it did not exist: British North America was a collection of separate British colonies, the largest of which was the Province of Canada. By the early 1850s, most of the

45. The pattern of landholding in a representative Ontario county is discussed in Gagan, *Hopeful Travellers*.

46. Lelièvre and Angers, *Questions Seigneuriales*, 1–4.

47. White, “Political Economy,” 35, 38.

colonies east of Lake Superior had achieved “Responsible Government.” Their autonomy in financial and monetary matters was not absolute, as the 1850s struggle between Canadian politicians and British civil servants over whether to adopt the dollar as the Province of Canada’s currency shows.⁴⁸ However, each colony had enough freedom to develop its own currency, financial regulations, and banking laws. On July 1, 1867, a federal state called the Dominion of Canada came into existence. The Dominion, which remained part of the British Empire, was vastly larger than its predecessor colonies. British Columbia’s entry into Confederation in 1871 gave Canada an outlet on the Pacific Ocean. Although this vast new supercolony was nominally a federation, Canada’s constitution was much more centralized than that of the United States, partly because Canada’s founding fathers had concluded that excessive decentralization had been one of the major causes of the Civil War in the United States.⁴⁹ Not surprisingly, the Canadian constitution of 1867 vested exclusive jurisdiction over banking with the federal government. At the constitutional convention in October 1864, this decision was non-controversial; the sole recorded statement about banking was a short declaration by Alexander Tilloch Galt, the Canadian finance minister, that “existing charters of banks” will “expire in 1870, when the subject may be reconsidered.”⁵⁰ The proclamation of the constitution initiated a debate about what sort of banking laws the combined colony should have, a debate that raged until 1871.⁵¹ At no point, however, did anyone question the right of the federal government to make banking laws, largely because the written constitution was so unequivocal about jurisdiction over this matter.

In contrast, ambiguity pervaded the sections of the United States Constitution related to money and banking. Under the terms of its 1787 constitution, Congress could pass legislation on banking only by invoking its hazy “Necessary and Proper” clause. Although the Constitution clearly prohibited the issue of paper money by the states,

48. This controversy is discussed in the Treasury Minute enclosed in Sir John Pakington to Lord Elgin, July 17, 1852, in *Appendix to the Eleventh Volume* Appendix P, 11–20.

49. Canada’s constitution was drafted in October 1864. Stevenson, *Ex Uno Plures*, 3–27. The best narrative history of the formation of the Canadian nation-state is still Morton, *The Critical Years*, 223–63.

50. Statement by Galt made at the Quebec Conference, October 21, 1864, in Pope, *Confederation*, 80.

51. Section 91 of the British North America Act of 1867 gave the federal parliament the exclusive authority to legislate in the following areas: “Currency and Coinage; Banking, Incorporation of Banks, and the Issue of Paper Money; Savings Banks; Weights and Measures; Bills of Exchange and Promissory Notes; Interest; Legal Tender.”

it was vague about whether the federal government had this power. It was also silent on the issue of jurisdiction over banking. As Hammond has suggested, this ambiguity was likely strategic, for while most members of the convention supported banking and a federal government capable of issuing bank charters, they recognized that public hostility to banking might be strong enough to “kill the chances of getting the constitution ratified.”⁵² Jurisdiction over banking under the US Constitution was unclear enough to cause a major debate over the constitutionality of the federal charter of the Second Bank of the United States. In the 1819 case of *McCulloch v. Maryland*, Chief Justice John Marshall ruled that Congress had the right to charter banks, even though the Constitution had not explicitly stated this. However, Jacksonian Democrats and other strict constructionists regarded Marshall’s ruling as illegitimate and continued to denounce the Bank on both economic and constitutional grounds. They frustrated the efforts to renew its charter, which expired in 1836.⁵³ During the Civil War, the right of Congress to charter and regulate banks was established but the right of state legislatures to do likewise was not extinguished, which meant that bankers could choose between state and federal charters. The existence of this dual system of state- and federally-chartered banks created regulatory competition and, according to some scholars, a “race to the bottom.”⁵⁴

In contrast to Canada’s relatively oligopolistic banking sector, the Gilded Age United States had a plethora of small banks. The 1863 National Bank Act, which established a system of federally chartered “national banks,” made it difficult for a national bank to establish branches in more than one town. Moreover, the capital requirements of the national banks were quite modest, just \$50,000 in a city with six thousand or fewer inhabitants and \$100,000 in larger communities. The result was a proliferation of national banks, over one thousand by 1865. Moreover, the 1863 banking law created niche markets for state-chartered and unincorporated banks because the national banks were prohibited from making mortgage loans. After 1863, the note-issuing national banks coexisted with a vast number of state-chartered and private banks.⁵⁵

While there is general agreement that the Canadian banking law of 1871 was important, historians differ as to why the Canadian parliament passed this law. Robert MacIntosh has recently depicted

52. Hammond, *Banks and Politics*, 105.

53. Ellis, *Aggressive Nationalism*, 204–5.

54. Scott, “Dual Banking,” 1.

55. Schultz and Caine, *Financial Development of the United States*, 316. The drafting of the National Banking Act is discussed in Blue, *Salmon P. Chase*, 157–60; Studenski and Krooss, *Financial History of the United States*, 154–5.

the contents of the 1871 legislation as the product of the disinterested deliberations of statesmen and academics.⁵⁶ MacIntosh's argument is plausible, but it minimizes the intense and highly self-interested political maneuverings that were going on behind the scene. D. C. Masters's 1941 article instead suggests that the 1871 legislation was the product of a political struggle between Canada's two largest cities for financial hegemony. Masters contrasts the 1869 banking law reforms, proposed when Sir John Rose, a Montréal financier, was still Finance Minister, with the banking laws of 1870 and 1871, drafted by Sir Francis Hincks, a Finance Minister from Ontario. For Masters, the 1871 law represented an attempt to balance the interests of the Montréal banks with those based in Toronto.⁵⁷

In the nineteenth century, Montréal was Canada's economic capital. Not surprisingly, banks based in the Province of Quebec represented 48 percent of the Dominion's paid-up banking capital in September 1867, even though Quebec was home to just 32 percent of the national population. Although eight out of ten Quebec residents spoke French, the English-speaking minority controlled the banking sector. Of Quebec's \$15.5 million in banking capital, the historically Francophone banks (Banque du Peuple, Banque Nationale, and Banque Jacques-Cartier) accounted for just \$3.5 million. Bank of Montréal shareholders and managers, who oversaw \$6 million in paid-up capital at Canada's largest bank, were English-speaking Protestants. Ontario, with 44 percent of the nation's population, provided just under 28 percent of the country's bank capital. Its largest bank, the Commercial Bank of the Midland District, had \$4 million in paid-up capital. The Bank of British North America (BBNA), an "imperial bank" chartered by the British government and headquartered in London, had a paid-up capital of £1,000,000 or \$4,867,000 in 1867. With branches throughout Canada, its assets represented 15 percent of all banking capital.⁵⁸ Masters is right to point out that the rivalry between Montréal and Toronto shaped the 1871 banking law. However, his interpretation overlooks the extent to

56. MacIntosh, "Origins of Financial Stability in Canada: The Bank Act of 1871," in *Relentless Change*, ed. Martin, 21–38. This piece expands on MacIntosh's earlier observations on the Bank Act of 1871 in *Different Drummers: Banking and Politics in Canada*, 11, 21, 32, 34.

57. Masters, "Toronto vs. Montréal the Struggle for Financial Hegemony, 1860–1875," 133–46.

58. Source of data regarding bank capital, Sessional Paper 12, "Statement in Obedience to the Order of the House of the 16th of March Last," in *Sessional Papers of the Dominion of Canada: First Session of the First Parliament, Session 1867-8*. Data regarding populations of provinces taken from Table A2-14, "Population of Canada, by Province, Census Dates, 1851 to 1976," *Historical Statistics of Canada* (Ottawa: Statistics Canada, 1983).

which there also was hostility toward Canada's emerging financial orthodoxy.

At this juncture, it is worthwhile briefly to consider how the rules Canada imposed on banks in this period both resembled and differed from those in the Australian colonies, the other major region of Anglophone settlement within the British Empire. One similarity between the Canadians and the Australians was that they both permitted branch banking.⁵⁹ It is true that by the 1860s, most of the British colonies in North America and Australia had achieved internal autonomy, which meant that their banking laws were now set by local legislatures, not by London.⁶⁰ Nevertheless, Britain continued to exert a powerful influence over banking laws in these colonies, not least because branches of banks headquartered in London and chartered by the imperial government could be found there.⁶¹ In Canada, the most important of the "imperial banks" was the BBNA, incorporated in London in 1836 and which quickly developed a network of branches.⁶² By 1859, several years before Confederation, its branch network extended from Nova Scotia on the Atlantic Coast to British Columbia on the Pacific.⁶³ This institution created an important precedent: since branch banks headquartered in London already existed in Canada, Canadian legislators would have found it difficult to deny the privilege of branching to local banks.

The very earliest Canadian bank charters had been silent on whether the banks were entitled to establish branches. Although no statute of incorporation specifically prohibited branching, two bank charters dating from New Brunswick in the 1820s implied that branches were not to be established, since the charters also authorized the directors to change the location (singular) of the bank. Of course, the charters of the Bank of Upper Canada (1819) and the Commercial Bank of the Midland District (1832) explicitly authorized branching, but these institutions were exceptional. Not until the early 1840s did it become standard practice to insert a clause explicitly authorizing branching into Canadian bank charters.⁶⁴ This change in the standard practice was likely a function of the arrival of the BBNA in the colony. In opting to continue to permit branch banking in 1871, the Canadian parliament was voting in favor of preserving what had been the status quo in Canada for over a generation.

59. Butlin, *Australian Monetary System*, 84–90.

60. Cochrane, *Colonial Ambition*, 35, 65–7, 283–91, 328.

61. Baster, *Imperial Banks*.

62. Young, *Upon the History, Principles, and Prospects*, Appendix A.

63. Neufeld, *The Financial System of Canada*, 461.

64. Hammond, *Banks and Politics*, 643, 660–2.

The Australians adopted three of the four pillars of Canadian financial orthodoxy: the adherence to the gold standard; the belief that interest charges should be set by market forces rather than being regulated by usury laws; and a firm belief that extensive borrowing in Britain would be essential to the growth of the colonies. One key difference between Canada and Australia was that the Australians did not seek to restrict access to the bank sector to firms with substantial amounts of capital. Instead, the Australians opted for a system of “free banking,” which resulted in the proliferation of small and lightly capitalized banks. Proponents of “free banking” argued that it would promote competition. According to the authors of the most recent work on the Australian bank panic of 1893, the Australian banking system in the late nineteenth century “had few legal barriers to entry, no branching restrictions and . . . no credible restrictions on assets, liabilities or bank capital, nor legally established price controls.” They argued that the lack of regulation implied by this system of free banking was the main reason for the spectacular collapse of the Australian banking system in that year.⁶⁵ An admirer of Canada’s 1871 banking law would probably argue that the 1893 crash could have been prevented had the Australians adopted all four, instead of just three, of the pillars of Canadian financial orthodoxy. The four pillars were indeed logically coherent. Adherence to the gold standard involved relatively strict limits on the expansion of the money supply and credit, something that was noted by the few Canadian advocates of a paper currency. The gold standard was fundamental to the importation of capital from the British Isles because it assured British investors that major currency fluctuations would not affect the value of their Canadian assets. Barry Eichengreen has shown that the prevalence of the gold standard facilitated international trade and investment by creating a *de facto* common currency.

The adherence of so many countries to the gold standard was only possible because unskilled workers, the social group that suffered the most from the associated tight monetary policies, did not have the right to vote in most nineteenth-century countries. Benjamin Disraeli’s 1867 franchise legislation in Britain was considered revolutionary because it doubled the size of the electorate from one to two million men, even though the country’s population was over twenty million.⁶⁶ As Britain and other countries expanded the franchise to include progressively more working-class men, the political basis of the gold standard was undermined. The United States, the first country to

65. Hickson and Turner, “Free Banking,” 151. Quote from 147.

66. Hall, *Defining the Victorian Nation*, 71.

extend the franchise to all (White) adult males, witnessed bitter debates about monetary policy and bimetallism in the decades after 1865. Although the United States resumed specie payments in 1879, there was anything but a consensus in favor of the gold standard in the United States after 1865. Indeed, each of the steps taken in preparation for the return to gold was bitterly contested by debtor classes.⁶⁷ The diffusion of American-style democracy to other Western countries also resulted in the spread of American-style monetary politics and with it, “Populist” hostility to the gold standard.⁶⁸

An old Canadian joke argues a color-blind man would be unable to tell the difference between the two major political parties: though the Liberals’ color is red and the Conservatives are blue, their policies are much the same. The kernel of truth in this joke is evident in the evolution of currency and banking law in the five years after 1867. When Sir John Rose, the Conservative Finance Minister, introduced his proposals in May 1869, he acknowledged that some members of both political parties opposed them. In other words, this was not a straightforward partisan issue.⁶⁹ Although they might differ on details, the leadership of the two major political parties in Canada subscribed to the same financial orthodoxy as did the major banks. In 1870, when the Conservative government introduced a law to outlaw charging more than 8 percent interest, the Prime Minister and the Finance Minister declared that they personally disagreed with the bill and were only introducing it at the behest of rank and file MPs. The leaders of the opposition Liberal Party, who also believed in “free trade in money,” then mocked the Prime Minister for introducing a bill in which he did not believe. The political elite and the financial *cognoscenti* in post-1867 Canada regarded usury laws and other populist, antifinancier measures as relics of a “barbarous age.”⁷⁰

Many ordinary Canadians in the late 1860s disagreed with one or more elements of the emerging financial orthodoxy. Their skepticism about banking and their downright hostility to international financial linkages echoes Jacksonian Democrats’ 1830s antagonism toward the Second Bank of the United States and its financial partners in London. The antifinancier group in Canadian politics disliked the money lending, big banks, and international financial markets that were

67. Ritter, *Goldbugs and Greenbacks*, 62–103.

68. Eichengreen, *Globalizing Capital: A History of the International Monetary System*, 29–31.

69. *Speech by the Honourable John Rose, Minister of Finance, on Introducing Resolutions on Banking and Currency*, 1.

70. See speeches by Sir Francis Hincks, 5 April 1870, *House of Commons Debates for 1870*, 869; Sir John A. Macdonald, *ibid*; 870, Alexander Mackenzie, *ibid*; 869.

increasingly important in Canadian life. A small but strident group of Canadians totally rejected the advanced technological civilization with which banks were associated. Others clearly supported railways and capitalist development but wanted tough restrictions on financial corporations which they regarded as a parasitical subspecies of business. Instead of oligopolistic banks, the gold standard, and market-based interest charges, they advocated soft money, usury controls, and laws making it easier for people to set up banks to compete with the incumbents.

There were effectively two debates about banking in Canada. On one level was the struggle within the federal cabinet about the precise regulations to be imposed on banks. All parties were financially orthodox. The disagreements about banking law within the federal cabinet and the banking community were relatively minor. For instance, some public men thought that Canada's currency should consist of notes payable in gold at the private banks, while others thought that the currency should consist of gold-backed notes issued by the government. Eventually, this dispute was resolved with the compromise that allowed private and government-issued notes to cocirculate. The key thing, however, was that both sides supported the gold standard. However, running alongside this narrow and technical debate among the elites was a popular discussion about the legitimacy of money lending and currency. The two debates intersected in the Canadian parliament, when opportunistic backbench MPs attempted to appeal to the antiusury sentiments of their constituents by denouncing financiers in fiery speeches. The populace's distrust of banking and financiers had a small but definite influence on Canada's post-1867 banking laws. It is probable that most Canadian adult males in 1871 would have favored legislation to restrict the concentration of financial power and to privilege debtors over creditors. The banking laws of 1870 and 1871 largely ignored their wishes.

Banking Legislation in British North America before 1867

Banking developed relatively late in British North America. The first banks in the United States emerged in Philadelphia and New York at the end of the American Revolution. Canada's first bank did not open its doors until 1817. On both sides of the border, the emergence of banks was regarded with suspicion by different parts of the community. For many of those engaged in "honest toil," the very concepts of paper money and people who derived livelihoods from handling it were anathema. Others recognized that banks were necessary but objected to what they regarded as the undue concentration of financial power in the hands of state-privileged corporations. In the 1830s, President

Andrew Jackson launched a war against the Second Bank of the United States, an institution he denounced as the pawn of sinister British investors.⁷¹ Jackson withdrew government deposits from the Bank of the United States and placed them in state-chartered banks known as the “pet banks.” His famous specie circular contributed to the financial panic of 1837.⁷²

In British North America, antificancier sentiment was also widespread. In Upper Canada, the future province of Ontario, the populist reformer William Lyon Mackenzie targeted the Bank of Upper Canada in the years before his unsuccessful rebellion against British rule in 1837. Mackenzie, who was against the very existence of banks, formed an unholy alliance with businessmen who wanted the legislature to charter more banks. Both Mackenzie and his newfound allies were against banking monopolies, although they disagreed over whether the best solution was to charter competing banks or to abolish banking altogether.⁷³ In Lower Canada, now Quebec, which also witnessed unsuccessful rebellions in 1837–1838, many French-speaking republicans disliked banks on general principles. Other Francophones resented the fact that the colony’s small English-speaking minority controlled the Bank of Montréal and, indeed, the economy as a whole.⁷⁴ The rebellions against British rule in Upper and Lower Canada were assisted by members of the hard-money and antibank Jacksonian “Locofocos,” who shared the rebels’ suspicions of banking and general worldview and supplied them with weapons and men.⁷⁵

In 1841, the colonies of Upper and Lower Canada united to form the Province of Canada. At this time, banknotes issued by a variety of banks circulated in the province, as did American, French, and British coins. Accounts were kept in a notional currency called “pounds currency,” which was worth somewhat less than sterling but subdivided in the same way. The first governor of the new province, Lord Sydenham, attempted to convince the colonial assembly to approve of a government bank of issue that would replace this monetary chaos with a single national currency. Opposition from the existing banks, which derived considerable profit from issuing notes, blocked this proposal.⁷⁶ In 1846, the Colonial Office in London issued

71. Austin, *Baring Brothers and the Birth of Modern Finance*, 93–105.

72. Hammond, *Banks and Politics in America from the Revolution to the Civil War*, 420–1, 455–6.

73. Craig, *Upper Canada*, 160–3.

74. Ouellet, *Lower Canada*, 132, 164, 236, 339; Rudin, *Banking en français*.

75. Bonthius, “Patriot War,” 16.

76. Shortt, “Currency and Banking, 1841–1867,” in *Canada and Its Provinces*, vol. 5, 261–94, 263.

a circular to colonial governors that encouraged the colonies to assimilate their banking practices toward those that had been established in England by Sir Robert Peel's 1844 banking law. It appears that the proliferation of banks and easy credit in the colonies had disturbed policy makers in London. William Gladstone as Colonial Secretary expressed concern that the lax banking practices in the colonies ran counter to the hard money doctrines then current in England.⁷⁷

In the late 1840s, demand rose for banking services in many Canadian communities, particularly in the newly settled districts west of Toronto. The existing chartered banks were unable to meet this demand because their charters imposed strict capital limits that impeded the creation of branches in financially marginal localities. In the late 1840s, William Hamilton Merritt, an American immigrant, began to champion "free banking" as a means to extend service to unbanked areas. Until that point, establishing a bank in Canada had required the passage of a charter by the legislature. Merritt proposed that Canada adopt New York State's 1838 banking law, which allowed anyone to open a bank, provided they could demonstrate to a registrar of banks that they had sufficient capital.⁷⁸ Despite predictions that free banking would lead to financial ruin, Canada's parliament passed a free banking law in 1850, which was swiftly followed by the opening of three small banks.⁷⁹

Canada's experience with free banking differed from that of the neighboring American states. Only three banks did business under Canada's free banking legislation and none of them developed reputations as bad as those of Michigan's "wildcat banks." Nevertheless, Britain's Colonial Office disliked the "free banking" law and attributed it to the unfortunate influence of the United States.⁸⁰ The Colonial Office was also displeased with the drift of

77. Knaplund, "James Stephen on Canadian Banking Laws, 1821–46," 177–187; Dowd, *The Experience of Free Banking*, 52; Butlin, *Foundations of the Australian Monetary System, 1788–1851*, 548 quoted in Hickson and Turner, "Free banking gone awry," 152.

78. *Agricultural Journal and Transactions of the Lower Canada Agricultural Society* 5 (January 1852), 20.

79. "An Act Respecting Banks and Freedom of Banking," *The Consolidated Statutes of Canada Proclaimed and Published under the Authority of the Act 22 Vict. Cap. 29, A.D. 1859* (Toronto: S. Derbishire and G. Desbarats, 1859), 647–5; Neufeld, *The Financial System of Canada*, 40–1. The three banks established under the terms of this legislation were Molsons Bank (which remained in operation until the 1920s), Zimmerman's Bank, and the Niagara District Bank. See Shortt, "Currency and Banking, 1841–1869," 273.

80. Memorandum by C. E. Trevelyan of the British Treasury, 11 July 1851, in *Appendix to the tenth volume of the journals of the Legislative Assembly of the Province of Canada*, Appendix ZZ, 2–4.

currency reform legislation in Canada. In 1850, Finance Minister Francis Hincks proposed that Canada abandon “pounds currency” and adopt a decimalized currency based on the American dollar. A bill to this effect this was passed by the Canadian parliament but was vetoed by the British government, which wanted Canada to adopt sterling.⁸¹ For the next four years, Canada’s Finance Minister engaged in a long-distance battle of wits with the Lords of the Treasury. The British Treasury wanted Canada to adopt the normal British currency, but said that it would tolerate a decimalized currency called the “Royal” based on the pound sterling. Eventually, Canada passed a law requiring government accounts to be kept in dollars and cents. Although some merchants in Canada had favored the adoption of sterling, Canada’s move to the dollar was pragmatic, consistent with signing a free trade agreement between the United States and British North America in 1854.⁸²

Although the United States became increasingly important to Canadians as an export market in the 1850s, Britain remained the major source for capital. British North Americans began borrowing in London for infrastructure in the 1830s, when Upper Canada needed money to complete the Welland Canal, which was designed to recapture commerce of the Great Lakes basin that had been lost to New York City and the Erie Canal route to the ocean. After 1841, the Province of Canada began a transportation revolution similar to the one underway in the United States. After the passage of the Railway Guarantee Act of 1849, Canada’s focus shifted to railways.⁸³ In addition to issuing its own bonds and guaranteeing those of the railways, the Canadian government underwrote municipal bond issues in the British market.⁸⁴ The direct and indirect debts of the Canadian government climbed from \$18.7 million in 1850, at the start of the railway building boom, to \$54.1 million in 1859.⁸⁵

Canada’s massive borrowing in England reawakened antifinancier sentiment in the colony. Many in Canada were increasingly

81. Sir John Pakington to Lord Elgin, 17 July 1852, enclosing a copy of a Treasury minute on the establishment of a uniform currency for British North America in *Appendix to the eleventh volume of the journals of the Legislative Assembly of the Province of Canada . . .*, Appendix P, 11–20, CIHM Reproduction 9_00955_11_3; Lord Elgin to the Legislative Assembly, 28 July 1851, *Appendix to the tenth volume of the journals of the Legislative Assembly of the Province of Canada*, Appendix YY, 1–13.

82. Adam Shortt, “Currency and Banking, 1841–1867,” 274–5.

83. Adam Shortt, “General Economic History, 1841–67,” in *Canada and Its Provinces*, vol. 5, 185–260, esp. 246.

84. Piva, *The Borrowing Process*, xiii.

85. Table No. 9, “Total Amount of the Public Debt,” in “Statistical Tables Relating to the Colonial and Other Possessions of the United Kingdom, 1860. Part VII,” in *House of Commons Parliamentary Papers* (London: HMSO, 1862), 67.

uncomfortable with their country's perceived dependence on the gentlemanly capitalists in the City of London.⁸⁶ Baring Brothers was attacked by a variety of Canadians, such as F. X. Garneau, a French Canadian nationalist writing in the early 1840s,⁸⁷ the *Toronto Globe*,⁸⁸ and the *Montréal Witness*.⁸⁹ Perhaps the most robust criticism of the London bankers came from pamphleteer Thomas Brothers, who agreed with Thomas Carlyle and John Ruskin that financial capitalism and industrial society had been a disaster for the workingman.⁹⁰ Brothers took his anti-industrial and antifinancier ideology to an idiosyncratic extreme. No newspaper editor or elected politician in British North America went so far in attacking financiers or capitalist modernity. Nevertheless, hostility to banking and moneylenders was present in both English-speaking and French Canada. For instance, in his famous 1864 novel *Jean Rivard*, Antoine Gérin-Lajoie associated the horrible practice of usury with the corrupting influence of luxury and fancy clothing. He warned his readers of what happened to unsuspecting rustics who went to town to sell their crops and then fell victim to "les usuriers."⁹¹

The presence of this strong current of antifinancier sentiment in Canadian political culture complicated the government's strategies for economic development. By the 1850s, the political class had become convinced that extensive borrowing in Britain was necessary. This approach caused several changes in Canada's banking laws. In 1854, Francis Hincks, a leading colonial politician and railway promoter, modified the banking laws to make it easier for Canadian banks to tap into British savings. The transfer and payment of dividends on bank stock in London was legitimized, as were large additions into the total authorized capital of chartered banks.⁹²

86. For the role of the gentlemanly capitalists of City of London in the governance of the British Empire, see *Gentlemanly Capitalism and British Imperialism*, ed. Dumett; *Gentlemanly Capitalism, Imperialism, and Global History*, ed. Akita.

87. Garneau, *Histoire du Canada*, 9:138.

88. Kerr, *A Scholarly Governor*, 192. For these allegations, see "Sir E. Head's Closet Councillors," *Globe*, August 7, 1858, 2. George Brown, the publisher of this newspaper, was not against the importation of capital from Britain. See his speech, 15 March 1860, *Thompson's Mirror of Parliament*, 8. However, he objected to the exercise of influence by the investors over Canadian politics.

89. "Confederation," *Montréal Witness*, January 19, 1867, 44.

90. Brothers, *A Letter to the Farmers and Working-Classes of Canada*.

91. Gérin-Lajoie, *Jean Rivard, économiste*, 76.

92. "An Act to Authorize an Addition to the Capital Stock of the Bank of Upper Canada and to Facilitate the Transfer of Shares" *Statutes of the Province of Canada . . . in the first session of the fifth Parliament of Canada*, 132, 140; "An Act to Amend and Consolidate the Several Acts Incorporating and Relating to the Bank of Montréal," in *Statutes of the Province of Canada passed . . . in the second session of the fifth Parliament of Canada*, 282.

Canadian legislators also tried to repeal the free banking law, a measure that would have brought Canada's financial legislation closer to that of England. In 1857, Alexander Tilloch Galt, a businessman who had previously been employed by a London-based free-standing company, proposed the repeal of the 1850 free banking law.⁹³ In 1860, Galt, then Finance Minister, recommended that the future growth of the banking system be through the extension of branch networks of the existing banks rather than through the creation of new banks.⁹⁴ Galt appears to have been influenced by Scotland's elaborate system of branch banking, which is not surprising given that his father, John Galt, was a prominent Scottish novelist and businessman.⁹⁵

Another way in which Canada's politicians attempted to assimilate the colony's banking laws to those of Britain was by emasculating the usury laws. For centuries, theologians' aversion to the charging of interest had reinforced the stigma against money lending throughout Christendom.⁹⁶ England started abolishing its usury laws in the 1830s, when a regime of "Free Trade in Money" was finally put into effect.⁹⁷ Their very last vestiges disappeared in 1854, when classical political economy and the ideal of *laissez-faire* were at the peak of their popularity.⁹⁸ In the United States, although some state legislatures repealed usury laws or allowed the courts to render them a dead letter, many states retained and tried to enforce their usury statutes. In Congress, where representatives of usury-law and free-trade-in-money states mixed, there were passionate debates about usury laws in the 1860s. Under the terms of the 1863 National Banking Act, the new federally regulated banks were prohibited from charging more than seven percent on loans.⁹⁹ In January 1867, Senator Henry Smith Lane of Indiana presented a petition asking "that the national banking law may be so amended" so that if a state's laws imposed a lower cap on interest rates, they should take precedence.¹⁰⁰

Canadians were torn between the example of free trade, free market Britain and the American model of imposing a legislative cap on

93. *Bill an Act to Discontinue the Incorporation of Joint Stock Banks and the Issue of Registered Bank-Notes, under the Free Banking Acts.*

94. Breckenridge, *Canadian Banking*, 161.

95. Timothy, *The Galts*, vol. 1.

96. For the history of usury laws in the Western world, see Nelson, *The Idea of Usury*.

97. See the legislative history of the usury laws of England in *Canadian Merchants' Magazine and Commercial Review*, "Usury Laws," August 1858, 315–17.

98. Hilton, *The Age of Atonement*, 95, 144, 263.

99. Schultz and Caine, *Financial Development*, 317.

100. See *Journal of the Senate of the United States*, January 19, 1867, 117. It should be noted that the legal rate of interest in Indiana at this time was 6 percent. See text of judge's decision in *Hogg v. Ruffner*, 1861.

interest rates. Popular opinion in many parts of Canada was hostile to financiers, but the polished gentlemen who dominated the Canadian politics were inclined to follow the British example. In Canada, lingering opposition to this idea of “Free Trade in Money” frustrated Francis Hincks’s and other legislators’ initial attempts to kill the usury laws.¹⁰¹ In 1847, the Trust and Loan Company of Upper Canada, a mortgage issuer based in England, complained to the British government about the persistence of Canadian restrictions on interest rates. Although Lord Grey, the Colonial Secretary, forwarded this letter to Governor Lord Elgin, along with a cover letter hinting that the usury laws ought to be repealed, no legislative action was taken at that time.¹⁰² Until 1853, Canadian law said that contracts between individuals to pay more than 6 percent per year interest were entirely void. This meant that if a debtor had borrowed money under such a contract, he could go to court and have the agreement torn up so that he did not have to pay anything back, including the principal. In 1853, the law was amended to say that contracts and securities were to be void only with respect to the excess of interest over 6 percent. In other words, the courts would enforce repayment of the principal and a moderate rate of interest.¹⁰³

Bank charters reflected the ancient prejudice against money lending and generally capped interest chargeable at 6 percent. Until 1858, Canadian banks attempting to secure more than 6 percent were liable to forfeit treble the value of the money lent. In such cases, half the money went to the Crown, the other half to the “victim” (i.e., the borrower).¹⁰⁴ A law passed by the Canadian legislature in 1858 established “Free Trade in Money” in loans between *natural persons*, meaning that individuals were free to negotiate whichever rates they pleased in a contract. For banking corporations, the maximum rate was raised to seven percent and the threat to the bank of losing both the interest and the principal on the loan was removed. To reflect the new maximum, the statute stipulated how short-term commercial paper should be discounted. For instance, for paper payable in thirty-one to sixty days, the maximum rate was set at 0.25 percent.¹⁰⁵

Judging from the debates in the Canadian parliament, the major motive for repealing or at least watering down the province’s usury laws was to “induce rich English, Irish, or Scottish capitalists to invest

101. See speech by Hincks, July 6, 1841, in *Mirror of Parliament*, 47.

102. See Lord Grey to Lord Elgin, 30 March 1847, enclosing letter from Robert Shank Atcheson dated 20 March 1847 in *Usury laws (Canada)*.

103. Breckenridge, *Canadian Banking*, 156.

104. *Ibid.*

105. Untitled, *New York Times*, August 19, 1858, 4; “An Act Respecting Interest,” in *The Consolidated Statutes of Canada*, 691–3.

their money in Canada.”¹⁰⁶ In introducing an 1846 bill to abolish the restrictions on usury, Solicitor General Henry Sherwood stressed that it was necessary to bring Canada’s laws into alignment with those that had been recently changed in England. He predicted that repealing the usury laws would encourage more British capital to enter the colony. Some opponents disputed that a capital influx would take place. For instance, Amable Berthelot, a French Canadian MP, spoke against lifting the existing 6 percent cap on interest, pointing out that “in England capitalists are often glad to get 3 or 4 per cent for their money.” He reasoned that if Englishmen had wanted to invest in Canada, they already would have done so under the existing laws.¹⁰⁷ Other legislators suggested that Canadians would get the short-term benefits of an influx of British capital but would end up as the peons of the investors. James Hervey Price predicted that “the money jobbers in a few years would be the owners of one half of the lands in Western Canada and the people the slaves of an aristocracy of all aristocracies the most hateful, a monied aristocracy.” Adding a dose of anti-Semitism to his speech, he declared that repealing the usury laws would transform Canadians into “Jews, shavers, and money jobbers.”¹⁰⁸

Robert MacIntosh has recently suggested that Canada’s usury laws had little practical effect on the business of banking. He reasons that since interest rates in the London money market were typically well below 6 percent, firms engaged in transatlantic interest rate arbitrage could still lend in Canada at a profit despite the cap on rates in Canada. He implies that the usury laws were of little practical importance and were more of a theoretical than an actual hindrance.¹⁰⁹ One can see why this conclusion made sense. First, Morton J. Horwitz has argued that case law rendered American usury statutes toothless in many states before the Civil War.¹¹⁰ As well, a recent study of 29,000 loans made by the Black River Bank of Watertown, New York, in the 1840s and 1850s shows that that this institution routinely evaded the state’s 7 percent interest limit.¹¹¹ It would be reasonable to conclude that conditions in Canada were similar to those in New York State.

106. “Usury Laws,” *Canadian Economist*, March 13, 1847, 365.

107. See speech by Berthelot, April 27, 1846 in *Mirror of Parliament*, 1846, 105.

108. See speech by Price, April 27, 1846 in *Mirror of Parliament*, 1846, 106.

109. MacIntosh “Origins of Financial Stability in Canada: The Bank Act of 1871,” in *Relentless Change*, 30–1.

110. Horwitz, *The Transformation of American Law*, 237–45.

111. A study of one New York State bank in this period suggests that usury laws “had little practical effect on lending behavior other than the general effect that high-risk borrowers were rationed when interest rates rose substantially above the usury ceiling.” Historian Howard Bodenhorn has shown that New York State’s 7 percent usury ceiling was routinely evaded by the Black River Bank. Bodenhorn, “Usury Ceilings,” 179–202.

However, there are several problems with the argument that Canada's usury laws were irrelevant to the practicalities of banking. First, the Bank of England's key interest rate sometimes went above 6 percent. It briefly hit 12 percent in the aftermath of the failure of the banking house Overend, Gurney, and Company in May 1866.¹¹² In November 1867, the rate in New York was between 10 and 12 percent.¹¹³ Even before this financial crisis, investors in the City of London had complained that Canada's usury laws were limiting their capacity to make loans.¹¹⁴ Second, the usury laws created litigation costs for Canadian banks. For instance, at the time of its collapse in October 1867, the Commercial Bank was engaged in a court battle with a debtor that centered on how judges ought to interpret the antiusury provisions in the bank's charter.¹¹⁵ The fact that Canadians vigorously argued about the wisdom of scrapping them indicates that the usury laws did, in fact, impinge on the business of lending money. After all, it would have been a waste of time to debate a dead-letter statute of zero practical relevance. Moreover, while Horwitz argued that the usury laws were a dead letter after 1820, usury laws in nineteenth-century American states had significant "real-world" consequences for both bankers and potential borrowers in those jurisdictions that actually enforced their usury laws. Not all American states had legislators and judges who were as relaxed about usury as those of New York were.¹¹⁶

During the 1860s, several legislators conducted an intermittent campaign to reestablish the usury laws. Joseph Cauchon, a French Canadian MP, introduced a bill in 1860 that would have made taking more than eight percent interest a crime punishable by imprisonment. George Brown, a rabidly anti-Catholic and anti-French businessman-politician from Toronto, pointed out that this law might well cause capitalists in the British Isles to avoid Canadian investments.¹¹⁷ As the American Civil War drew to a close, Canadian demands for a usury law increased, probably because of the economic hardships

112. *Blackwood's Edinburgh Magazine*, "The Panic in the City," July 1866: 78–93, 79, 87; Collins "Overend Gurney Crisis, 1866," in *The New Palgrave Dictionary of Money and Finance*, ed. Newman.

113. *Monetary Times*, "Money and Trade," November 14, 1867, 100.

114. *Bankers' Magazine* [London], "Bank of British North America," July 1865, 846–8.

115. For the case of *Commercial Bank v. Cotton*, see *Monetary Times*, November 21, 1867, 108.

116. Benmelech and Moskowitz, "The Political Economy of Financial Regulation."

117. Speeches by Joseph Cauchon, George Brown, 15 March 1860, in *Thompson's Mirror of Parliament*, 7–8.

caused by the war and the Americans' termination of their free trade agreement with Canada in 1865. The US 1863 National Banking Act probably also lent legitimacy to Canadian demands for a usury law since that statute prohibited federally regulated banks from charging more than 7 percent on loans.¹¹⁸ In 1865, a proposal emerged to lower the legal maximum rate of interest in the Province of Canada to 6 percent for all lenders, corporations as well as natural persons.¹¹⁹ In 1865, John Sandfield Macdonald, who had served as Premier of the Province of Canada between 1862 and 1864, informed the Canadian parliament of his opposition "to what is called free-trade in money." Macdonald argued that "moneyed corporations" such as the "Trust and Loan Company" were harming the province by draining profits back to Britain. He wanted to do something to protect Canadian farmers from this menace and usury laws were the answer.¹²⁰ J. B. E. Dorion, a French Canadian politician from the left-wing and quasi-republican *parti rouge*, suggested that "nine-tenths" of the French Canadians favored usury laws. Dorion said that unwillingness of the government to respect the will of the populace and introduce such laws was a sign that it was undemocratic.¹²¹

British investors complained about the usury laws of the other British North American colonies. Moaning about the Province of Canada's usury law was heard at the June 1866 Annual General Meeting in London of the Trust and Loan Company.¹²² Capitalists in Britain also denounced interest controls in Nova Scotia and New Brunswick, which were even more stringent. In 1864, Charles Dickinson Archibald, a Nova Scotia businessman living in London, asked New Brunswick politician Leonard Tilley to repeal his province's usury laws. Archibald argued that they were obsolete in an age in which most countries allowed "the laws of supply and demand" to determine the price of money. Until the New Brunswick laws ended, the province would "remain a terra incognita to capitalists. I could at this moment divert large sums to the lower provinces if there was free trade in money."¹²³

118. Schultz and Caine, *Financial Development*, 317.

119. See *An Act to Amend the Act Respecting Interest*.

120. *Parliamentary Debates on the Subject of the Confederation of the British North American Provinces*, March 7, 1865, 738.

121. *Ibid.*, March 9, 1865, 859.

122. *Daily News*, [London] June 1, 1866, *Canadian News* [London], "Commercial," June 7, 1866, 365. The charter of the Trust and Loan Company, which issued mortgages in Canada, limited interest to 8 percent.

123. The usury laws of New Brunswick and Nova Scotia were considered even worse by some people in London. See C. D. Archibald to Tilley, dated London 3 March 1864, Library and Archives Canada, Samuel Leonard Tilley Fonds 17.

In the 1850s, it had been relatively easy for Canadians to borrow in London because interest costs had been low and there was political stability in North America. After the attack on Fort Sumter, British investors became hesitant about putting more money into Canada. During the Trent Affair in December 1861, it appeared as if the North might declare war on Britain and invade Canada. Lincoln decided to fight “one war at a time” and arranged a diplomatic solution of the Trent Affair, but not before the British army had rushed thousands of troops to Canada. Trade dislocations caused by the Civil War also cut the Canadian government’s revenue. Border raids by Confederate agents operating in Canada disrupted Canada’s exports, as did the expression of pro-Confederate sympathies by prominent Canadians and the introduction of a passport requirement for travel to the United States. The appreciation of Canada’s gold-based currency relative to the American “greenback” also made it harder to export to the United States, especially after the value of the US currency fell to just 36 cents Canadian.¹²⁴ Faced with rising borrowing costs in London and a growing deficit, Canada’s politicians searched for financial expedients. One of them was to borrow money from the Bank of Montréal, Canada’s largest bank.

The growing dependence of the Canadian government on the Bank of Montréal led to accusations that its general manager, Edwin King, was exercising an undue influence over the government.¹²⁵ King was unpopular because he was a strong proponent of hard money and had a relatively conservative approach to credit. King believed that many of the banks west of Toronto had been profligate in extending credit. Following the English currency school’s doctrine of “real bills,” King believed that banks should only extend credit to borrowers who provided collateral in the form of stationary goods or warehouse receipts. People in the still underdeveloped western counties, who had fewer goods they could use as collateral and where easy credit and the autumnal expansion of the money supply were crucial to moving crops to market, despised King’s theory that banks should not lend to an individual simply on the strength of his name.¹²⁶ King’s

124. This was in July 1863. See Schultz and Caine, *Financial Development*, 324.

125. Denison, *Canada’s First Bank*, vol. 2, 142. Born in 1828 in Ireland, King had come to Canada to work in the Montréal office of the BBNA. In 1857, he had defected to the Bank of Montréal, where he had risen to general manager by 1863. In 1869, he became president of that bank, an office he held until 1873 when retired from active business and returned to the United Kingdom. He died in Monte Carlo in 1896. See Ronald Rudin, “E. H. King,” *Dictionary of Canadian Biography*.

126. Breckenridge, *Canadian Banking*, 224. For the development of the “real bills doctrine” in King’s native England, see Smith, “On Central Banking ‘Rules,’” 39–61.

proposals came to be regarded with even greater suspicion in the districts west of Toronto in 1866, when the Bank of Montréal withdrew accommodation from grain handlers and other merchants in Upper Canada in order to speculate on the price of gold on Wall Street.¹²⁷

Accusations that King was the real power behind the throne intensified in 1866 when Finance Minister Galt unveiled a plan to reduce the government's deficit by issuing a provincial currency. Under Galt's scheme, the chartered banks would have eventually lost their right to issue their own banknotes, which he would replace with Provincial Notes. Eight million dollars in specie would back up these notes, which be redeemable at designated government offices. This plan would have reduced the money supply and allowed the government to collect the profits from issuing banknotes which the chartered banks had previously enjoyed.¹²⁸ King favored Galt's plan because it would have allowed him to convert the debt the government owed to the Bank of Montréal into banknotes. The legislature passed the Provincial Notes Act, along with a statute relieving banks of the remaining penalties for charging more than 7 percent interest.¹²⁹

Although its aim was to deprive the chartered banks of the seignorage they derived from issuing currency, Galt's scheme would have preserved Canada's adherence to the gold standard. Indeed, by tightening up the money supply, it would have moved Canada closer to the hard money principles that had been supreme in England since the passage of Sir Robert Peel's 1844 Bank Act. Galt's proposal was a slap in the face to the many Canadians who had been advocating a softer currency for several years. Since the early 1850s, a group of merchants and politicians known as a "rag baby party" had been agitating for the introduction of an inconvertible paper currency.¹³⁰

127. Adam Shortt, "Banking System of Canada," in *Canada and Its Provinces*, vol. 10, 637. The Bank of Montréal does not appear to have withdrawn accommodation in Lower Canada, which used a very different legal system based on the custom of Paris. The Montréal banks had long complained about "unjust" laws in Upper Canada that favored debtors over creditors and which were injurious to the "Banking interest." In the aftermath of the financial crisis of 1857, William Workman, president of the City Bank, had complained that these laws compelled banks to "relinquish collateral securities or accept terms of settlement of the dictation of the debtor himself, which in Lower Canada they could have refused." See Workman's report to the shareholders in "Annual Meeting of Stockholders, City Bank, June 1858," in *The Canadian Merchants' Magazine and Commercial Review* 3 (June 1858), 221. The Bank of Montréal's New York trading operations are discussed in Denison, *Canada's First Bank*, 160–2.

128. *Act to Provide for the Issue of Provincial Notes* (Ottawa: G. E. Desbarats, 1866).

129. Adam Shortt, "Currency and Banking, 1841–1867," 284–6; Breckenridge, *Canadian Banking*, 177–8.

130. Shortt, "Currency and Banking, 1841–1867," 282.

One of the most eloquent spokesmen for this group was Isaac Buchanan, a prominent conservative and protectionist.¹³¹ In an 1865 pamphlet outlining the economic case for Confederation, Buchanan presented colonial political union, internal free trade, and protective tariffs directed against the outside world as logical corollaries. He sought to abolish all tariffs within British North America while simultaneously creating a high tariff around the new federation. Buchanan also argued that the new country should adopt a non-convertible paper currency because devaluation would boost exports and encourage local manufacturers.¹³² Others in British North America agreed with Buchanan that leaving the gold standard for a fiat currency would be good idea.¹³³ One protectionist magazine, the *Canadian Quarterly Review*, praised the iron currency that the lawmakers of ancient Sparta had introduced for the express purpose of rendering external trade difficult.¹³⁴ Canada would never have adopted gigantic iron coins, but had the Dominion abandoned the gold standard in the 1860s, shifting to a greenback-style currency, the country's international commerce would have been disrupted. Still, local factory owners, who resented that Canadians were importing so many manufactured goods from overseas, likely would have seen a positive aspect in such a turn of events.

Legislative Developments: 1867–1871

In fall 1866, the Bank of Upper Canada closed its doors. Its problems stemmed from a combination of the effects of a tightened money supply in Upper Canada, a series of bad loans that the bank had made for political reasons, and the transfer of the government's lucrative account to its archrival, the Bank of Montréal. The achievement of Confederation on July 1, 1867, was swiftly followed by another banking crisis in Ontario, an October run on banks in the Toronto area. The crisis, which generated queues of panicky depositors, did not abate until the government used the telegraph to announce that it

131. McCalla, "Isaac Buchanan," *Dictionary of Canadian Biography*.

132. Buchanan, *The Relations of the Industry of Canada*.

133. See testimony of Isaac Buchanan in the Minutes of Evidence of the "First Report Select Committee on Currency and Banking," *Journals of the House of Commons of Canada from April 15th to June 22nd 1869*, A1–13; "Inconvertible Currency," *Canadian Merchants Magazine and Commercial Review*, August 1857, 421; "Curse or Blessing," *Montréal Trade Review*, March 24, 1865, 117.

134. "A National Currency," *Canadian Quarterly Review and Family Magazine*, April 1864, 139–51. The post-Confederation politics of currency are discussed in Rich, "The Gold-Reserve Requirement under the Dominion Notes Act," 447–53.

would continue to accept the notes of the affected banks at face value for taxes and other payments. Before the crisis subsided, the Commercial Bank of the Midland District, which had unwisely invested in the bonds of the Detroit and Milwaukee Railway, was forced to suspend.¹³⁵ In the days preceding suspension, the directors had sought cash from a variety of quarters. Finance Minister Galt pressured the Bank of Montréal to participate in a private-sector rescue package. Edwin King reluctantly agreed to attend a meeting of leading bankers and politicians that was held in the Montréal offices of the BBNA, but then essentially refused to join in helping the Commercial.¹³⁶ Galt then asked his cabinet colleagues to authorize granting \$500,000 in assistance to the Commercial Bank, arguing that there would be a widespread panic if it failed, so the taxpayer needed to step in. Sir John A. Macdonald, the prime minister, refused to authorize a government bail out, and the bank was forced to suspend operations. Galt felt betrayed by Macdonald and resigned from the cabinet in November 1867.¹³⁷ The failure of the Commercial Bank had endangered Galt's own personal finances.¹³⁸ As Galt euphemistically explained in his resignation speech, "private affairs of importance required his attention at the present time."¹³⁹ It should be noted that Macdonald's decision not to help the Commercial stemmed not from a lack of sympathy for its plight, for he had served as a director and the bank's solicitor since 1839. Moreover, the bank was headquartered in Macdonald's own parliamentary constituency of Kingston, which was devastated by the failure of its premier financial institution. However, Macdonald thought that the shareholders in solvent Montréal banks within his own party and the wider Canadian public would revolt if they learned he had used their taxes to prop up a bank that had extended him many soft loans.¹⁴⁰

135. "The Suspension of the Commercial Bank of Canada," *Montréal Trade Review*, October 25, 1867. A Toronto-based account of the suspension of this bank is provided in: "The Commercial Bank," *Monetary Times*, October 10, 1867, 60; *ibid*; October 3, 1867, 53; *ibid*, "Lessons of the Crisis," October 31, 1867, 84; *ibid*, "Our Banking System," November 14, 1867, 100. See also Shortt, "Currency and Banking, 1841–1867," 290.

136. According to Merrill Denison, the Bank of Montréal provided one short-term loan but then balked at providing additional assistance to the Bank of Upper Canada. Denison, *Canada's First Bank*, 150–2.

137. "Sir Alexander Tilloch Galt," *Dictionary of Canadian Biography*.

138. Galt to Sir John A. Macdonald, 1 November 1867, Library and Archives Canada, Sir Alexander Tilloch Galt Fonds, MG27-ID8, vol. 3, 1217.

139. *Montréal Trade Review and Intercolonial Journal of Commerce*, "Mr. Galt's Resignation," November 15, 1867, 690.

140. Martin, *Favourite Son*, 25–7, 101–3, 180–2, 185–8.

The Commercial Bank's failure proved awkward for the government, as the Prime Minister owed the bank a sizeable sum. Macdonald, who had recently been knighted and married, had borrowed extensively to live in the style to which he had become accustomed. In June 1866, Macdonald had gone from being "Mr. Macdonald" to "Sir John," which created certain expectations about how he should present himself. In May 1867, Macdonald's debts reached \$64,000, most of which was owed to the Commercial Bank of Canada. The bank had long refrained from pressing the issue of repayment because of Macdonald's position as both Prime Minister and one of its directors. An investigation of the Commercial Bank's liabilities after it suspended found that the bank was essentially sound, except for the one bad investment in the Detroit and Milwaukee (\$942,672) and the smaller loans to Macdonald. In a deal brokered by the government, the Merchants' Bank of Montréal agreed to take over its assets and liabilities. This arrangement preserved the depositors' accounts and even gave the shareholders something for their equity. Sir Hugh Allan, president of the Merchants' Bank, noted that one of the major assets he had acquired was Macdonald's debt but did not pressure Macdonald. Instead, he politely said that it would be nice if the Prime Minister could attend to the matter of the debt. Macdonald was able to borrow some money from Senator D. L. Macpherson for this purpose, but was unable to repay most of the money he owed Allan. Hewitt Bernard, Macdonald's brother-in-law, negotiated a settlement of the outstanding debts for just \$6,100 in 1872, at which point Sir Hugh Allan was negotiating with the government for the charter to build Canada's transcontinental railway.¹⁴¹ It is reasonably clear that Allan's generous decision to forgive much of Macdonald's personal debt was connected to the railway charter, which was itself the center of the affair that destroyed Macdonald's government in the next year.¹⁴² The Canadian Pacific Scandal of 1873, which has many similarities to the *Crédit Mobilier* scandal in the United States, is a reminder that legislative capture and outright corruption were common on both sides of the forty-ninth parallel.¹⁴³

In November 1867, Sir John Rose, a Montréal businessman replaced Galt as Finance Minister. In 1868, the Canadian Parliament passed "An Act Respecting Banks" that extended all existing the bank charters and regulations. This law also gave banks established in any

141. Young and Tulchinsky, "Sir Hugh Allan," *Dictionary of Canadian Biography*; Johnson and Waite, "Macdonald," *Dictionary of Canadian Biography*.

142. Martin, *Favourite Son*, 95–6, 101–12.

143. Kens, "Crédit Mobilier."

province an absolute right to operate throughout the federation. The 1868 banking law was a stop-gap measure, designed to give Rose time to design a true national banking law for the new federation. In 1869, Rose extended the banks' charters for another twelve months, pending the "final settlement of the banking and currency question."¹⁴⁴ Rose then got to work on the details of Canada's new banking and currency laws. He frequently consulted with E. H. King, an admirer of the 1863 National Banking Act in the United States. In 1869, the need for a final settlement of the banking and currency questions became more urgent. The influential *Montréal Trade Review* suggested that uncertainty over this issue was damaging commercial confidence and predicted that the passage of a new banking law would lead to a "two-fold" increase in Canadian banking capital.¹⁴⁵ At this very moment, the United States was experiencing convulsions over its own banking system because the constitutionality of the greenbacks instituted during the Civil War was being challenged in various appellate courts with some success.¹⁴⁶ In February 1870, US Supreme Court Chief Justice Salmon Chase declared parts of the Civil War currency legislation unconstitutional, which sent shockwaves through markets. Ironically, Chase had been the US Treasury Secretary at the time the legislation in question had been passed.¹⁴⁷ This growing atmosphere of crisis and uncertainty about the value of North American banknotes demanded decisive action on the part of the Canadian parliament.

When Rose presented his banking scheme in the House of Commons on May 14, 1869, he emphasized the need for financial uniformity in all provinces. He noted that few of the forty-two banks in the Dominion operated under precisely the same regulations. Nova Scotia had neither reserve requirements nor restrictions on the number of notes a bank could issue, aside from a confusing stipulation that the total liabilities of a bank could not exceed three times the combined amount of the paid-up capital and customers' deposits. Rose said that at the time of its failure, the Bank of Upper Canada had \$2.6 million in liabilities and just \$39,000 in specie. The only thing that had cushioned the impact of the bank's failure on note holders had been the law saying that the notes of a failed bank were still legal tender for the purposes of repaying debts. The capital requirements of

144. *Montréal Trade Review*, "Bank Charters," June 25, 1869, 391.

145. *Montréal Trade Review*, "The Banking System of the Dominion," July 2, 1869, 408. Given that this publication was connected to Erastus Wiman, the head of Canadian operations of R. G. Dun and Company, a credit-reporting agency, it seems like a particularly credible source of information on commercial confidence. For Wiman's career, see Grant, "Erastus Wiman," 1–20.

146. Unger, *The Greenback Era*, 172–4.

147. Blue, *Chase*, 304–5.

most banks were, according to Rose, insufficient, and the problem was only going to get worse as improved transportation reduced the costs of transport. Previously, isolation had forced bankers in the several provinces to be more cautious, since their banknotes had circulated primarily in the localities in which the personal reputations of the directors were at stake. With the increasing ease of travel and the formation of a transcontinental polity, bank managers would be tempted to overextend their note issues and to take other risks. Rose reasoned that a bank director would be less concerned about leaving the note holders high and dry if the bank's notes were dispersed from the Atlantic to the Pacific rather than being concentrated in the hands of his neighbors.

Rose planned a swift termination of the right of banks to issue their own paper money and the creation of a national currency convertible into specie at government offices. This design also involved the "safeguard" of raising the capital requirements for banks. Banks would have to have a nominal capital of at least one million dollars, of which 20 percent would have to be paid up before the bank could open its doors for business. At this stage, Rose also proposed capital ratio requirements, a rule that Canada did not impose on its banks until 1934. Rose praised the national banking system that Salmon P. Chase had developed in the United States and credited the Americans' new federal tax on the currency issues of the state-chartered banks with having eliminated the dubious banknotes that had complicated commerce on both sides of the border before 1863. Rose reminded his listeners that all merchants had been required to keep a directory of banknotes as thick as a "Family Bible" on their tills so they could evaluate the current market worth of such notes as the "shinplasters" of Michigan, the despicable "red-dogs" of Indiana and Nebraska, and the miserable "stump-tails" of Illinois and Wisconsin.¹⁴⁸

Parliamentary debate over Rose's plan took place on June 1, 1869. Opponents of the scheme charged that it would limit competition by hampering would-be bankers who had less capital.¹⁴⁹ Some critics suggested that the Bank of Montréal, the bank with the most capital, would be the major beneficiary of the new regulations. Others suggested that Rose's plan would unduly restrict the money supply and would cause problems for both creditors and communities in

148. *Speech by the Honourable John Rose, Minister of Finance*, 10.

149. We lack a transcript of the debate. It appears that some sort of verbatim record of the debate in the Commons was made, but even D. L. Macpherson, a member of the upper house, complained about being unable to get his hands on it. See Macpherson, *A Letter to John Rose*, 1. The reasons why the transcript of the debate went unpublished have never been made clear.

which the money supply needed to expand dramatically with each fall harvest. Perhaps the most forceful critic of the legislation was D. L. Macpherson, a Toronto businessman who sat in Canada's unelected upper house. Senator Macpherson praised Canada's pre-1866 banking system as the best in the world, with the possible exception of the Scottish banking system on which it had been modeled. Macpherson said that no Canadian bank had ever failed prior to the 1866 Provincial Note Act, the statute that had, in his eyes, caused the problems of the Bank of Upper Canada and the Commercial Bank. He said that the legislation proposed by Rose would be unlikely to achieve the two major *desiderata* the government had established, namely, security for note holders and the creation of a national currency of uniform value. Macpherson held that that it was impossible for a banknote to command a perfectly uniform value in a large country, since the express charges involved in converting paper money into specie would inevitably reduce the value of notes issued in the distant locales.¹⁵⁰ Moreover, he said, three recent financial crises in England (1847, 1857, and 1866) showed that banknotes issued by the government were less safe than notes issued by private banks.¹⁵¹ He suggested that note holders in England would have enjoyed greater security under the pre-1844 Scottish currency and banking laws and that Canada's should be left unchanged.¹⁵²

Rose's proposal evoked outrage in Ontario, where many regarded the existing banking law with the sort of respect typically reserved in that region for the teachings of John Knox. The *Toronto Leader*, normally a reliably pro-Conservative paper, denounced it as "certain to lead to disastrous consequences."¹⁵³ There were public petitions against changing the system and rumors of a split within Sir John A. Macdonald's cabinet. To no one's astonishment, the Bank of Montréal liked Rose's proposal, as did the BBNA, operating under a British charter. However, the bankers of Halifax and Ontario detested the proposal because it would have restricted the money supply.¹⁵⁴ In the midst of this political firestorm, Rose suddenly resigned as Finance Minister.¹⁵⁵ He moved to London, where he pursued a successful career selling North American railway securities.¹⁵⁶ From Britain, he

150. Macpherson, *A Letter to John Rose*, 6.

151. *Ibid.*; 9.

152. *Ibid.*; 10.

153. *Toronto Leader*, "The Banking Question," May 14, 1869, 2. In 1870, the paper said that had they been implemented, Rose's proposals would have been the "shipwreck" of the Conservative government. See *Toronto Leader*, April 1, 1870, 2.

154. Shortt, "Banking System of Canada," 629.

155. Creighton, *John A. Macdonald*, vol. 2, 37.

156. Farr, "Sir John Rose," *Dictionary of Canadian Biography*.

continued to advise Macdonald on Canada's banking law. In December 1869, Rose received Edwin King in his offices in the City of London to discuss the banking law that had been proposed by Sir Francis Hincks, Rose's successor as Finance Minister. Unfortunately, the memorandum that Rose enclosed in a letter to Macdonald has not survived, so it is hard to determine whether he had much influence over the banking act that Hincks eventually drafted.¹⁵⁷

Sir Francis, who replaced Rose as Finance Minister, had left Canadian politics in 1856 when the British government had appointed him governor of Barbados. Hincks's career as a colonial governor had come to an abrupt end in 1869 due to a squabble with a mercantile clique in Guyana, his last posting. Suddenly unemployed, Hincks decided to visit Canada. Fortuitously, his return to the country coincided with Rose's resignation as Finance Minister and Macdonald's desperate search for a replacement. Although he did not have a seat in the Canadian parliament, Hincks had financial experience, which suited him for the position of Minister of Finance. Macdonald appointed him to the post in 1869 and, echoing British practice, he was soon elected to represent a constituency located in Ontario, yet close enough to the provincial border to fall within Montréal's commercial orbit.¹⁵⁸

Toronto merchants had criticized Rose's proposal as excessively favorable to the Montréal banks. Learning from Rose's political mistakes, Hincks constructed the compromise plan that became the banking law of 1870. This statute did not abolish the right of the banks to issue their own notes, as Rose had proposed, but it did keep them from issuing notes worth less than four dollars.¹⁵⁹ The law provided for a government bank of issue for smaller denominations. Hincks increased the capital requirements for banks, although not as much as Rose had envisioned: He modified Rose's bill by changing the minimal capital requirement from 1 million dollars to \$500,000, 40 percent of which had been paid up before a bank could begin

157. Rose to Macdonald, 21 December 1869, in Library and Archives Canada, Sir John A. Macdonald Fonds, microfilm C-1522, 40364–7; Rose to Macdonald, 23 December 1869, C-1522, 40368–9.

158. Hincks, *Address on the Banking System of Canada*, 5; Longley, *Sir Francis Hincks*, 350–5.

159. Hincks's preference would have been to make the issue of bank notes a government monopoly. In an 1873 pamphlet, Hincks described Sir Robert Peel's 1844 Bank Act as imperfect because "it permitted the continued issue of Bank Notes by English private and Joint Stock banks and by Scotch and Irish banks." Hincks, *The Bank of England*, 5. In 1871, Hincks appears to have considered legislating a minimum cash reserve for banks, but soon dropped this idea after all of the banks made their opposition clear. A cash reserve was imposed in 1934 at the same time Canada decided to create a central bank. Neufeld, *Financial System*, 106.

trading.¹⁶⁰ In 1871, Hincks made some slight modifications to the 1870 banking law: the second statute authorized the federal government to take over the government-run savings banks that had been established in Nova Scotia and New Brunswick before 1867.¹⁶¹ Hincks simultaneously arranged for the passage of a national currency law that established a uniform currency and affirmed Canada's commitment to the gold standard. Thereafter, a British sovereign would be worth precisely 4.8667 Canadian dollars.¹⁶² This meant that when the United States resumed specie payments, the Canadian and American currencies would be at par. After 1880, British and American coins cocirculated in Canada, along with special Canadian coins produced by the Royal Mint in London and private mints in Birmingham.¹⁶³

The reforms enumerated above reflected the financial orthodoxy that had become the consensus among Canada's economic and political elite. Only one feature of the post-1867 regulatory environment reflected the antibanking sentiment in the general population: the Canadian parliament opted to extend the pre-1867 interest laws that existed in some provinces. In 1870, Sir Francis Hincks introduced a bill that would have established a uniform national law regulating usury. Hincks's law would have limited interest to 8 percent on loans between natural persons but would not have lifted the restrictions on interest contained in bank charters. In Nova Scotia, a pre-Confederation statute limiting interest charges to 6 percent per annum was still in effect, whereas in the former Province of Canada (i.e., Ontario and Quebec), the principle of "Free Trade in Money" applied to loans made by natural persons, although not to those made by banks. Hincks stated that while he personally wanted to abolish all vestiges of the usury laws, the opposition to this idea in Nova Scotia and Quebec made it necessary to introduce the "reasonable compromise" he was now proposing.¹⁶⁴

Hincks's speech initiated a fierce debate in the House of Commons that did not respect partisan lines. In this debate, Sir George-Étienne Cartier, a Cabinet colleague, challenged Hincks's insinuation that all

160. *Toronto Leader*, "Parliament Yesterday," April 1, 1870, 2; Breckenridge, *Canadian Banking*, 248; Denison, *Canada's First Bank*, 167–9.

161. Breckenridge, *Canadian Banking*, 258. These banks were incorporated in the Post Office Savings Bank. Neufeld, *Canada's Financial Development*, 47. For the government-run savings banks, see Bunbury, "Safe Haven for the Poor?," 24–48.

162. The British sovereign remained the standard of value in Canada until the establishment of Royal Canadian Mint in Ottawa in 1908. Shortt, "Banking System of Canada," 650.

163. Breckenridge, *Canadian Banking*, 259.

164. Canada, House of Commons, *Debates*, 1st Parliament, 3rd session, April 6, 1870, 906.

French Canadians supported stringent usury laws, pointing out that he personally favored Free Trade in Money, a policy opposed by some English speakers in Ontario.¹⁶⁵ The truth of Cartier's statement was borne out when the Premier of Ontario, Sandfield Macdonald, spoke up in favor of usury laws. Other MPs objected to the bill because it did not apply to banking corporations, which would be allowed to charge only the rates stipulated in their charters.¹⁶⁶ When Mackenzie Bowell, a prominent Conservative and future Prime Minister, said that every state in the Union had usury laws and that Canada should follow their lead, Alexander Mackenzie, another future Prime Minister, pointed out that the usury laws were dead-letter statutes in New York State.¹⁶⁷ MPs from Nova Scotia denounced the bill because it would immediately add two percent to their constituents' borrowing costs.

The sensitivity that Hincks showed to the feelings of the Nova Scotians on the question of the usury laws needs to be understood in the context of the federal government's ongoing efforts to reconcile that province to being part of the Canadian federation. Most people in Nova Scotia had opposed the act of the British parliament incorporating their colony into Canada. Moreover, the launching of the Canadian federation had been swiftly followed by the election of a secessionist provincial government in Nova Scotia. Most of the MPs elected by Nova Scotia to the first federal parliament in September 1867 were secessionists who took their seats affirming that their sojourn in Ottawa would be a short one. They wanted Nova Scotia to be released from the federation so that it would be able to control all of its own laws. By 1868, the state of unrest had reached the point that free-lance military adventurers in the United States were expressing an interest in launching a raid to "liberate" Nova Scotia from British/Canadian rule. Although such offers of military assistance were rebuffed by Nova Scotia's Attorney General, there were those in the Halifax who declared that they would prefer annexation to the United States over remaining in Canada.¹⁶⁸

Canada's government attempted to defuse the situation in Nova Scotia with modifications of the tariff and other policies calculated to appease the moderate antisecessionists. In an astute political maneuver, Prime Minister Macdonald effectively bribed Joseph

165. Hincks was not the only person to attribute the usury bill to Quebec. An editorial in the *Toronto Globe*, a francophobic and rabidly anti-Catholic paper blamed Hincks's retrograde usury legislation on the influence of the French Canadian MPs. See "Cheap Money by Act of Parliament," *Toronto Globe*, April 25, 1870, 2.

166. Canada, House of Commons, *Debates*, 1st Parliament, 3rd session, April 6, 1870, 906.

167. *Toronto Globe*, "Rate of Interest," April 6, 1870, 4.

168. Harvey, "Incidents of Repeal Agitation in Nova Scotia," 48–57.

Howe, the leader of Nova Scotia's secessionist movement, into accepting Confederation by offering him a position in the Canadian cabinet.¹⁶⁹ Dislike of Canada's relatively high tariff was the major reason driving Nova Scotian secessionism, but the currency question also contributed to the unrest. Until 1869, the British sovereign had a legal tender value of 500 cents in Nova Scotia and just 486.67 cents in central Canada.¹⁷⁰ Nova Scotians complained that the federal government's plan to apply the central Canadian standard to them would have involved a deflation of 3 percent in Nova Scotia, a measure that would have benefited creditors and penalized debtors who had entered into contracts under the old currency. Currency legislation thus pitted capitalists against debtors in Nova Scotia. Given that it had just imposed a deflationary policy on Nova Scotia, it was probably wise for the federal government to shelve its plans for the complete assimilation of the usury laws of the several provinces by acquiescing in the continuance of a law that many Nova Scotians saw as helpful to debtors. The federal government's ongoing strategy of reconciling Nova Scotia to Confederation helps to explain why Hincks, normally a strong believer in free trade in money, introduced a usury bill in 1870.

Due to opposition from a tactical alliance of those who regarded Hincks's proposed law as insufficiently stringent and politicians who were dogmatically committed to "Free Trade in Money," the legislation failed to pass.¹⁷¹ A secessionist newspaper in Halifax reported this news with glee, seeing the failure of Hincks's measure as yet another sign that the federal government was losing its "adhesive power."¹⁷² Toronto's *Monetary Times* regarded this turn of events as the least bad scenario, remarking that while uniformity of laws was a noble ideal, it was better to permit Nova Scotia to keep its usury law than to abandon Free Trade in Money in the more populous provinces of Ontario and Quebec. Reopening the question of the usury laws in central Canada would be dangerous, it said, because doing so might permit the French Canadians to impose their backward views on the rest of the Dominion. Quebec, the paper reported, "places the bills of the Pope above the most irrefragable arguments of Bentham and the whole body of the economists."¹⁷³ Thereafter, the Dominion passed province-specific legislation that perpetuated the diversity of laws

169. Pryke, *Nova Scotia and Confederation 1864-74*, 84.

170. "The Currency," *Montréal Trade Review*, December 6, 1867, 739.

171. Canada, House of Commons, *Debates*, 1st Parliament, 3rd session, (1870), April 22, 1870, 1145.

172. "A Back-Down Government," *Halifax Morning Chronicle*, April 29, 1870, 2.

173. "Uniformity of Laws: Usury," *Monetary Times*, May 6, 1870, 596.

confronting the chartered banks, trust companies and private lenders of money.¹⁷⁴ The extent to which these rules actually affected the business of banking is not clear, but an 1888 handbook of Canadian banking law devoted six pages to explaining these complex statutes, which suggests they were indeed more than dead-letter statutes.¹⁷⁵

In the last quarter of the nineteenth century, the currency question continued to agitate politics in the United States. Terms such as bimetallism, greenbacks, resumption, and the “Cross of Gold” joined the political lexicon.¹⁷⁶ In Canada, however, monetary and banking questions ceased to be lively.¹⁷⁷ Both the gold standard and the basic provisions of the 1871 banking act became part of the political consensus. Even when Canada’s overall output contracted dramatically in the aftermath of the financial crash of 1873, the consensus remained in place. The essential principles of the 1871 banking act were perpetuated when renewing bank charters in 1880, 1891, and 1901. In the 1870s and 1880s, Canadians debated a variety of ways of rescuing their country from the financial doldrums. Many people latched onto the idea of the protectionism, which was implemented with the passage of the so-called National Policy tariff in 1879.¹⁷⁸ Others regarded a free trade agreement with or even incorporation into the United States as the panacea for all of Canada’s problems. More trade with the other regions of the British Empire was the pet project of a third group. There were also those in Canada who subscribed to the views of Henry George or the Marxian socialists.¹⁷⁹

What is striking about the period from 1871 to 1914 is that there was no major movement to change the currency or financial system of Canada. William Jennings Bryan had no analogue in Canadian politics. Financial orthodoxy had triumphed in Canada in a way that it had not in the United States. Not until the meteoric rise of the Social Credit movement in the Province of Alberta in the 1930s did monetary or banking questions become contested issues in Canadian electoral politics.¹⁸⁰ By then, Canada had something close to universal

174. “An Act Respecting Interest and Usury in the Province of Nova Scotia,” 36 Vic., chap. 71, in Davidson, *A Compilation of the Statutes Passed since Confederation Relating to Banks and Banking*, 72.

175. Weir, *The Law and Practice of Banking Corporations under Dominion Acts*, 415–20.

176. See Cherney, *A Righteous Cause*, 24–107; Ritter, *Goldbugs and Greenbacks*.

177. There were a few stray individuals in Canada who proposed leaving the gold standard, but they never formed a real political movement. Goodwin, *Canadian Economic Thought*, 83–6.

178. Forster, *A Conjunction of Interests*.

179. Bliss, *A Living Profit*; McKay, *Reasoning Otherwise*, 84–6.

180. For the monetary policies of early Social Credit, see Hesketh, *Major Douglas*.

adult suffrage, which allowed quasi-Populist political movements to have a greater say in lawmaking. Moreover, Canada's political system had come to resemble that of the United States in another way, with the appearance of a Canadian version of the doctrine of "states' rights." The intention of the creators of the Canadian constitution of 1867 had been that the lion's share of power would rest with the federal government. This goal had been frustrated by a series of judicial decisions after 1881 that effectively transferred authority of several key areas of economic policy from Ottawa to the provincial governments.¹⁸¹ In this new constitutional environment, it is not surprising that American-style political debates about banks would appear north of the border.

CONCLUSIONS

The creation of a national banking law was an important event in Canadian history because it led to transcontinental branch banking, which sharply distinguished Canada from the United States. Oligopoly, extensive branching, and relative stability characterized post-1871 Canadian banking, whereas the United States had many small unit banks, intense competition, and frequent banking crises. Although some of the features of post-1871 Canadian banking were already evident in 1871, the banking law of that year was important because it solidified, amplified, and legitimated trends that were already under way. Given the importance of this legislation, it is not surprising that contemporaries vigorously debated these laws. One dimension of this struggle was the fight within the Canadian federal cabinet about the precise details of the banking law. Even so, all parties subscribed to the emerging financial orthodoxy. The four elements of this financial orthodoxy were: oligopolistic banking, adherence to the gold standard, the belief that interest charges should be set by market forces rather than by usury laws, and the belief that that British, rather than domestic or American, savings, should remain the engine of Canadian economic growth.

Running alongside this debate among elites was a popular discourse about money lending and currency. In the 1860s, much of the Canadian populace evidenced a strong distrust of banking and financiers. For better or worse, the attitudes of Canada's agrarian majority had a limited impact on the making of the banking law of 1871. The 1871 law was just one of several factors that influenced the

181. Stevenson, *Ex Uno Plures*, 278–300.

evolution of Canada's banking sector after Confederation. It would be simplistic to attribute the stability of banks in twentieth and twenty-first century Canada entirely to this law or even to regulation in general. However, in accounting for the stability of Canada's financial system, an important place must be accorded to the regulatory framework developed in the protean days of the Canadian federation. As this essay has shown, the 1871 banking law was both a crucial moment in Canadian financial history and a key part of Canadian nation-state formation.

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