

Since the first banks were established during the first quarter of the nineteenth century,* the commercial banking system has developed in response to the changing needs of the Canadian economy, an evolution which is still in rapid progress today. Canadian economic development has been characterized by two main features—successive but by no means continuous periods of rapid geographical expansion of settlement, and a continued dependence on export markets as new natural resources (agricultural land, forests and minerals) were exploited. Thus, Canadian banking has continually had to migrate to new areas and to find appropriate methods of financing new industries and new products; and it has from the beginning possessed a strongly “international” character† with a good deal of emphasis on the financing of foreign trade, on foreign exchange operations, and on correspondent relations with foreign banks. At the same time, as the regional isolation which was so marked in British North America before Confederation has gradually broken down and the economy has been integrated, the Canadian banks, originating in local areas, have become part of a nation-wide banking system, in part by process of amalgamation which was particularly marked in the first twenty-five years of the present century.

Bank Legislation

From the first, banks in what is now Canada sought to operate under Acts of incorporation (charters) passed by the legislatures of the colonies in which they operated. As new banks were incorporated and older ones obtained charter renewals, there developed in the bank charters themselves a quite extensive and fairly uniform code of banking law. This occurred partly because the colonial authorities in Britain (until about 1840) endeavoured to have certain general rules and safeguards inserted in all charters, and partly in response to developing Canadian experience in banking. At Confederation, responsibility for banking and currency was given to the Dominion Government and in 1871 the first general Bank Act was passed. This legislation is subject to review and revision every ten years, a feature that has helped to keep the banking system adapted to the needs of a changing economy.

From this historical process certain characteristic features of the Canadian financial system have emerged—notably the traditional emphasis of the chartered banks on “commercial” banking. The provision of mortgage funds and long-term industrial capital and the performance of trust functions were for the most part left to the other financial institutions which gradually developed. The early banks were established by merchants for merchants. Their note issues provided a badly needed medium of internal exchange and they advanced working capital to finance the processes of trade. The aim was to make lending as far as possible short-term and self-liquidating. The bank charters from the first contained prohibitions against lending on the security of real property, except as secondary or subsequent security. This continued to be a feature of Canadian banking law and was, indeed, well suited to a system where liquidity of assets was very necessary because the banks’ liabilities were mainly of a very short-term character, i.e., notes and deposits paid on demand. (The banks’ note issues were long the most important part of the circulating medium of the country. They continued to issue notes until after the Bank of Canada was created in 1935, when their note-issuing privilege was gradually withdrawn.) Now, however, exceptions to the rule against lending upon security of real property, incorporated in the Bank Act in 1944 and 1954, allow the banks to participate in government-guaranteed loans to farmers and fishermen and for housing constructed under the National Housing Act, to lend to oil companies on the security of oil “in, under or upon the ground” and production equipment, and to extend their consumer-finance lending by taking chattel mortgages.

Another distinctive feature of Canadian bank lending arrangements is that contained in Sect. 88 of the Bank Act. This, too, is an exception to the rule against lending on the security of goods and property and was developed over a long period to facilitate particular

* See introductory paragraph to Section 3.

† The larger Canadian banks have long maintained offices in London and New York. In addition, some Canadian banks for more than half a century have been providing an important part of commercial banking facilities in the Caribbean area. See Table 10, p. 1122.