The problem of rural credits in the United States

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1915

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THE PROBLEM OF RURAL CREDITS IN THE UNITED STATES

A THESIS

submitted in partial fulfillment
of the requirements for the
degree of Master of Arts

BY

Harold Howard Maynard

June 1915

The State University of Iowa
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American economists and statesmen have been interested in European systems of cooperative credit for many years, and have considered the possibility of introducing similar systems into the United States. However, it was not until 1912 that any definite action was taken having this end in view. In that year the three great political parties each declared in favor of some improved system of rural credits, and demanded legislation authorizing the establishment of such a system in the United States. Earlier in the same year (1912) President Taft asked Ambassador Herrick, then a resident in Paris, to investigate the French and German credit unions and land mortgage banks, and report as to their practicability in the United States. Mr. Herrick complied with this request, and submitted his report late in the same year. President Taft submitted this report to the Conference of Governors in session at Colorado Springs, Colorado, in December, 1912, and at the same time sent them a letter asking that they take some action looking toward the improvement of credit facilities for American farmers. The governors saw the need of better credit facilities and appointed a committee to study the credit situation, and report at their next meeting to be held at Richmond, Virginia, a year later. The committee submitted its report at this meeting and after some discussion another committee was appointed to draft a bill for the estab-
lishment of systems of rural credits. It was thought that such a bill could be passed by all the state legislatures. The committee appointed for this purpose, after much consideration of the matter, decided that it would be impossible to draft a bill which could become a law in every state, and so reported to the governors when they met at Madison, Wisconsin, in December, 1914. However, the report of the committee discussed the principles which must be followed in establishing state systems of credit unions, which they recommended should be formed under state authority. They recommended that the mortgage banks be established as a federal system, which should supplement the Federal Reserve System of commercial banking.

The attention of the people of the United States was further drawn to the subject of rural credits by a meeting of the Southern Commercial Congress at Nashville, Tennessee, in the spring of 1912. One of the chief speakers before this convention was Mr. David Lubin, the American delegate to the International Institute of Agriculture of Rome, Italy. Mr. Lubin described the Raiffeisen and Schultze -- Delitzsch unions as well as other forms of cooperative credit associations, and advocated the establishment of similar systems in the United States. The members of the Congress were much impressed by this address and passed a resolution authorizing the appointment of a commission from among its members to go to Europe and study the various systems of credit and report as to their
practicability. Before this commission could sail for Europe, it was changed to the American Commission by the addition of delegates from each state and some of the Canadian provinces. This commission went to Europe in May, 1913, and made a careful investigation of the various rural credit systems in use on the continent as well as in Great Britain and Ireland. Their report was submitted early in 1914 and was later supplemented by reports from a committee in each state regarding the need for improved credit facilities. The committees to make these reports had been appointed by the various state governors at the request of the American Commission.

The submission of the report of the American commission together with the expressed wish of President Wilson, that something be done towards bettering rural credit conditions, served to center the attention of Congress on this type of legislation. Joint sessions of the Banking and Currency committees of the House and Senate were held between February 16th and March 18th, 1914. During that time witnesses from all sections of the country were examined as to the need for better rural credit facilities. These witnesses included several members of the American Commission, who had investigated conditions in Europe with respect to credit facilities. After considering the information obtained from these witnesses,
the committees drafted the Hollis-Bulkeley bill which provided for the formation of a complete system of land mortgage banks. This bill was referred to the proper committee in each house on May 13th, but owing to the pressure of other business, it was not recommended for passage by either committee. When Congress met in December, 1914, President Wilson advised in his annual message that the time which could be devoted to the consideration of any rural credits legislation was short, and that nothing should be done towards establishing a system of rural credit. Notwithstanding this advice, when the Agricultural Appropriations bill passed the Senate on February 25, 1915, it contained a provision for lending the funds of the government to the farmers for long time loans. When the bill reached the House, this amendment was not approved; and in its stead the House passed the Hollis-Bulkeley bill which was called from the committee and passed without discussion. Both the amendment to the Appropriations bill and the Hollis-Bulkeley bill were subsequently killed by the conference committee of the two houses, and as a result the last Congress accomplished nothing towards the solution of the rural credits problem.

This is in brief the history of the movement which is seeking to solve the problem of providing an improved and efficient credit system for the farmers of the United States.
Before discussing the problem in detail, a view of the entire field is necessary. European systems of credit include two general types of associations. The first of these, of which the German Landschaften and the Credit Foncier of France are types, are organized for the purpose of providing a method whereby the farmer may secure funds to purchase land or to improve land already owned, pledging the land purchased as security. Funds for this purpose are obtained by the sale of bonds based on the mortgages given, as security. The farmer is allowed to repay his loan by the payment of a stated amount at each interest paying date. The second type of associations is illustrated by the Raiffeisen unions of Germany. They have for their purpose the granting of small loans to the farmers of their district. The loans are used to improve the farm, to buy new equipment or for any productive purpose. The security given is generally the promissory note of the borrower.

It is not the purpose of this paper to present a discussion of all the systems of credit unions and land mortgage banks, but rather to describe some of the more important features of a few typical systems, both in the United States and abroad. This discussion will be followed by a survey of the credit conditions in different parts of the United States; and the last chapter will consider the plan of mortgage banks proposed by the Hollis-Bulkeley bill.
I

LAND MORTGAGE INSTITUTIONS IN EUROPEAN COUNTRIES

Section 1

The Landschaften or Mortgage Associations
of Germany

Long time loans for agricultural purposes in Germany
are obtained through the Landschaften or mortgage associations.
There are many forms of these associations, and although each
type has some distinctive features, they are all based on the
same principles. The origin of these mortgage associations
can be traced back to the time of Frederick the Great, when the
first association was established by his order on August 29th, 1769.¹ The chief purpose of this first association was the
relief of the nobles who had lost their property during the
Seven Years War, and who needed credit to repurchase their
estates. The association provided a means whereby they could
pledge their united property, and thus secure the needed credit.
The first association was soon followed by others, all of which
depended upon increasing the available supply of credit by the
issue of paper money based upon the land of the members as se­
curity, rather than by the sale of bonds. The plans adopted
did not provide for the amortization of the loan, nor did they
provide for the collection of the interest by the association.

¹ Herrick's Rural Credits, p. 43.
In short, they were merely an intermediary between debtor and creditor, and their chief interest is that they formed the basis for the present efficient system.

Possibly the best and most successful of the present associations is the one operating in the province of Silesia. Although it is connected with the government, and some of the others are not, it can be considered atypical association and hence is used as an illustration of the workings of the plan. The province of Silesia is divided into nine districts and each of these is sub-divided to form the territory of a local mortgage association. The local association is the basis of the entire system, but the locals are united into district associations, which, in turn, are united into one general association for the entire province. Each local association has a manager elected from among its own members; an executive committee; and an attorney, the latter being the only officer to receive pay for his work. Semi-annual meetings are held for the transaction of business requiring general action. All landowners in the community are eligible for membership, honesty and industry not being essential qualifications, as in the Raiffesen associations for short time credit, where these qualities are often the only securities given for a loan.

A loan is obtained by a member of the association through application to the executive committee of the local, stating the object to which the money will be put and the time for which
it is desired. The property to be mortgaged by the applicant is then appraised by a special committee appointed for the purpose, and if the object of the loan is approved, an amount not over two-thirds of the value of the property will be lent to the applicant. The loan is secured by a first mortgage, which is given to the local association and held by them until the principal of the loan is repaid. Bonds are then issued by the association, secured by all of the mortgages which it owns, and additional funds are thus obtained to meet the demands of the stockholders for loans. As the mortgages cannot represent more than two-thirds of the value of the property mortgaged, and as the total bond issue cannot be more than the value of the mortgages held by the association, the bonds are a safe investment. The bonds are issued in denominations ranging from $25 to $1,000, and are not issued for a definite term of years, but are redeemable upon the advertised call of the issuing association or by purchase in the open market. Coupons are attached for the payment of interest, which is paid by the mortgage association from funds collected from the borrowers.

When the borrower makes the application for the loan, he states the period for which he wishes to use the money, which period may vary from ten to seventy-five years. The officers then determine what his annual payment shall be, basing their

1 Morman's Principles of Rural Credits, p. 83.
calculation upon the rate of interest paid on the bonds issued and on the time for which the loan is made. This annual payment is made up of three funds. The annual interest is the first of the funds; the payment of the principal is the second; and the third is a small payment of the running expenses of the association. Figured for the average period of 53 years, this annuity will be about four and one half per cent of the principal, but on loans for short terms it will amount to five or six per cent of the principal. Should the borrower wish to repay the entire loan or any part of it, he may do so at any interest paying date. Payment may be made in cash or in bonds of the association. If the borrower pays cash, the association uses it to redeem bonds, thus maintaining the same relation between the bonds and the loans of the association.

An account is kept with each borrower showing the amount of the annual payment and the part of it which goes to each of the three funds mentioned above. In this way, the borrower has a constantly increasing fund to his credit, which, when the loan is matured, will equal the original amount loaned. The debt will then be discharged and the mortgage cancelled. Loans are made to non-members of the association upon application and appraisal of their property as in the case of members, and all loans made to them are recallable by giving six

1 Metcalf's Rural Credits in Germany, p. 16.

2 Rural Credits in Germany, 63rd Congress, 2nd Session, Senate Document No. 571, p. 20.
months notice. Figures given below will show that these loans are much smaller, in general, than are loans made to members.

The system has proved so satisfactory that there is no trouble in disposing of the bonds issued, as they furnish a safe as well as a convenient form of investment. They generally sell about par, going above or below as the market conditions affect them.

In 1912, the 3½%'s sold for from 91.8 to 94% of their face value, and the 4%'s sold as high as 101% of their face value.¹

For the year 1912, the business of the association in Silesia, was as follows:²

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount loaned to members</td>
<td>850,162</td>
</tr>
<tr>
<td>Amount loaned to non-members</td>
<td>875,881</td>
</tr>
<tr>
<td>Smallest loan</td>
<td>23.81</td>
</tr>
<tr>
<td>Largest loan</td>
<td>59,525</td>
</tr>
<tr>
<td>Outstanding loans to members</td>
<td>97,912,505</td>
</tr>
<tr>
<td>Outstanding loans to non-members</td>
<td>52,409,294</td>
</tr>
<tr>
<td>Total outstanding loans</td>
<td>150,328,899</td>
</tr>
<tr>
<td>Bonds issued</td>
<td>150,338,890</td>
</tr>
<tr>
<td>Mortgages held to secure loans to members</td>
<td>1,818</td>
</tr>
<tr>
<td>Mortgages held to secure loans to non-members</td>
<td>59,996</td>
</tr>
</tbody>
</table>

This is but an illustration of the work done by one of the many land mortgage associations. Each has its special rules, but the two fundamental principles of organization are the same. These are first, the lending of funds obtained from the sale of bonds based upon mortgages on the estates of the

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¹ Herrick's *Rural Credits*, p. 76.
² Herrick's *Rural Credits*, pp. 74, 75.
borrowing members; and second, the amortization of the debt by annual payments. Neither of these principles has as yet been generally applied to agriculture in the United States and it is difficult for Americans to realize the significance of the movement looking towards their adoption. The principles have proved to be workable under widely different circumstances and conditions, and the adoption of some system embodying them is probable in the United States in the near future.

Section 2

The Credit Foncier of France

The struggle for a satisfactory system of agricultural credit in France has been long and severe. The first half of the 19th century was marked by many attempts to establish a satisfactory system of long time mortgage loans, but none was successful. Early in 1852, an act was passed authorizing the establishment of land mortgage banks in all parts of France. Many banks of this type were formed, but before the year was ended the law was changed and all the banks which had been organized were consolidated into one central bank. This bank, known as the Credit Foncier, was given a monopoly of the land mortgage business of France for twenty-five years, and a direct aid of $2,000,000. As organized at present, it is a share institution, the capital being $45,000,000. This is divided
into shares of $100 each, which sold on the Bourse for $146 in 1910. The officers of the bank are a president appointed by the President of France, vice-presidents and a board of directors elected by an assembly of the two hundred largest stockholders.

The funds raised from the sale of capital stock are not used primarily for loanable capital, but are held as a reserve against the bonds of the bank issued to meet the demand for loanable funds. Because the capital is held as a reserve, one half of it is kept invested in fluid securities and the other one half is used to buy commercial paper of various kinds or is lent on mortgages. Dividends on the stock are limited to six per cent; the remainder of the profits, if any, going into a reserve fund which is invested at the discretion of the board of directors. Private savings or commercial deposits are accepted up to $20,000,000 and are lent on mortgages.

The prime purpose of the bank is the lending of money on long time mortgages running from ten to seventy-five years. These mortgages must be amortized by annual payments and cannot be paid before the maturity of the loan. Besides these long time loans, loans running less than ten years are made.

1 Herrick's Preliminary Report to President Taft, p. 22.
2 Herrick's Rural Credits, p. 117.
3 Interviews of the Monetary Commission, p. 283.
4 Interviews of the Monetary Commission, p. 271.
5 Mormon's Principles of Rural Credits, p. 135.
These are amortizable or not at the pleasure of the borrower. The entire principal of these short time loans or any part of it may be paid at any interest paying date. Loans to municipalities and to drainage districts are also made by the Credit Foncier.

The interest charged on loans is at present 4.3%. If a loan of $100 is to be repaid in ten years, an annual payment of $12.41 will pay both principal and interest.\(^1\) If it is to run twenty-five years, the annual payment will be $6.56. If the period is fifty years, the payment will be $4.88, and if it runs seventy-five years, the payment will be but $4.66 per year.\(^2\)

Any resident of France, either urban or rural can obtain a loan upon application and proof that his property is free from incumbrance. The amount lent is limited to one-half the value of the property and in the case of vineyards or forests which are liable to rapid depreciation, only one-third of the value of the estate can be lent. The property mortgaged must have a steady income as large as the annuity to be paid. A first mortgage is given to the bank as security. Bonds are issued upon these mortgages and are sold in the open market as in the German Landschaften. The bonds are of four classes corresponding to the four classes of loans mentioned above. They are issued in series of from $50,000,000 to $180,000,000

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1 Haskin's *Articles on Rural Credits*, p. 28.
2 *Interview of National Monetary Commission*, p. 234.
and have no fixed date of maturity. They are redeemed by purchase in the open market or by retirement by lot. The ones retired in this way are advertised by number and at once cease to draw interest. Prizes increasing the face value of certain of the bonds from $300 to $400 are given. The bonds to receive the prizes are selected by a drawing conducted by the governor of the bank. These prizes as well as the fact that the bonds, although bearing only three per cent interest, sell in the Bourse at such a rate that they will net about four per cent, make the demand for them by investors, very active. In fact, the issue of three per cent in 1912, amounting to $100,000,000 was over subscribed eighteen times.

Although not purely a cooperative mortgage association, the Credit Foncier embodies many of the cooperative principles and besides seems to be the type of organization which could be used under American conditions. Its success goes to show that the idea of selling bonds to secure funds to loan on farm lands, is workable and that when properly organized to meet a definite need, a system embodying it will succeed.

Section 3

Land Mortgage Institutions in Italy

For the last half century, Italy has been endeavoring to establish a satisfactory system of land mortgage banks, but has
been unsuccessful until recent years. Many laws have been passed authorizing the establishment of various types of institutions, but experience soon showed that the Associations would not prove to be successful and the laws were repealed. As a result, the present mortgage business is confined to two types of institutions both of which seem to be successful.

The first agency for granting long time loans is the mortgage department of the savings banks in the country towns. This is a separate department having its own officers, capital and reserves. The capital and reserves are loaned and other funds are obtained by the sale of bonds. These bonds are issued without limitation except that the total must not be greater than the entire amount of the loans made by the bank. The bonds bear from three and one-half to four per cent interest and are redeemable upon call. The mortgages are amortized by annual payments as in Germany. In fact they are the German Landschaften associations adapted to Italian conditions, by being made a part of a bank which does a regular banking business.

The second Italian institution for granting mortgage credit is the "Land Credit Company of Italy", which was organized in 1890. It is a large central institution doing business in all parts of the country. It has a capital of

1 Herrick's Rural Credits, p. 142.
2 Herrick's Rural Credits, p. 144.
$20,000,000, held jointly by the government and by private citizens. It uses this capital for loans but increases the amount available for that purpose by the sale of bonds. In 1912 it held loans amounting to $733,246,124.¹

Section 4

Other European Loan Banks

There are in Germany, besides the Landschaften described above, many other banks which issue real estate mortgages, but which are relatively unimportant. The rural savings banks hold a large number of second mortgages on farms already mortgaged to one of the Landschaften for two-fifths of their value. These mortgages held by the savings banks are not a basis of bond issue, nor are they subject to amortization in most cases. The insurance companies of Germany, as in the United States, have a large part of their reserves invested in mortgages, but only a small portion of these are on land. In 1912 there were 38² stock banks known as land credit banks which were organized in an effort to compete with the Landschaften, but which have been unsuccessful because of the difficulty of selling a recallable bond except by a long established institution. These banks have succeeded in placing only about one-sixth of their mortgages on farm lands.

Austria has a system of provincial mortgage associations

¹ Herrick's Rural Credits, p. 148.
² Herrick's Rural Credits, p. 103.
in all but two of her provinces. These associations are owned and controlled by the provincial governments and furnish funds for real estate mortgages. They sell bonds to secure the funds lent. The credit of the province is also frequently used to borrow still further to lend to the farmers of the province. Only amortizable long time loans are granted, the length of the loans varying from thirty to sixty years. The average time for which they run is fifty-four years, and in this time the principal can be repaid by an annual payment of four and one-half per cent. Hungary also has a very successful bank known as The Land Credit Institution. It is a cooperative institution doing a general banking business as well as granting long time loans repayable by amortization.

In Russia the Peasants State Bank is the source of long time mortgage loans. This bank is a state owned and controlled institution which was formed to take over the lands sold to the government by the nobility during the troubles of 1905, when they feared confiscation of their property by the peasants. It has adopted the policy of selling the lands to the ex-serfs, taking a first mortgage as security. It also issues debenture bonds and uses the funds obtained to help the peasants in many ways. It has been a very powerful factor in establishing the former serfs on the farm lands.

Switzerland has a very successful system of land credit
institutions similar to Germany. The Scandinavian countries also have adopted the German form of organization and have used it successfully.
II

SOME EXAMPLES OF EUROPEAN COOPERATIVE CREDIT UNIONS

Section 1

The Raiffeisen Credit Unions

Any study of the Raiffeisen system of banks must necessarily consider the life and character of its founder, for without an understanding of the motives and principles of his life, we cannot understand the basic principles of the system which bears his name. F. W. Raiffeisen was born in Germany in 1818. His education was directed with a view of entering the military department of the government, but before his studies were completed, eye trouble compelled him to change his plans and enter the civil service. Although nearly blind he was able to render efficient service in this field. His first post was as mayor or burgomaster of a small town, Weyerbuck, in a poverty stricken forest district. Here the condition of the peasants, always bad, but intensified by the famine years, 1848-1849, made an everlasting impression upon him; and he determined to do something to better their condition.

It is difficult for us to understand and appreciate the terrible condition of the German peasant class of that time. Perhaps the one word, usury, describes it better than any other.

1 Wolff's Peoples' Banks, p. 71.
The peasants were in the grasp of the money lender. The farm, crops, livestock, and even the house furniture were frequently all pledged to the usurer and life was a struggle to keep from losing the little that they had. The land yielded but little, because of lack of proper tools and fertilizers, and opportunities for earning money away from the farm were very limited. The German laws favored foreclosure, and many a farmer lost his all in this way. Credit was essential, but could only be obtained from the usurer. Usury laws, police regulations, and warnings all failed, and the peasants were helpless.

Raiffeisen was transferred to a slightly better town in 1848, and here the opportunity to help improve the condition of the peasants came. His first step was the organization of a cooperative bakery, which was soon followed by a livestock purchase association. This attacked one of the strongholds of the Jews, the purchase and sale of livestock, but they still held their control over the money market. After a great deal of effort, Raiffeisen succeeded in borrowing $1,500 and with this as capital he opened the first cooperative credit union. Credit was to be granted as a charitable undertaking without regard to the feasibility of making the union financially successful. Experience soon taught that this was more demoralizing to the recipient of the loan than it was helpful, and the reorganization of the union on business principles soon
followed. This first cooperative credit society was formed in 1849, but not until 1854 was the second organized, and not until 1880 did the associations begin to multiply rapidly. During this period, Raiffeisen tried out many schemes and modified the original plan in many ways, but the fundamental principles were correct, and since 1880, the growth in the number of societies has been rapid.

The system of cooperative credit unions is founded on two fundamental principles. The first principle is that of cooperative credit, or borrowing money on the strength of the combined resources of the members of the association; and the second is the unlimited liability of all the members of the association for its debts. In other words, Raiffeisen believed that industry, frugality, sobriety and honesty were a proper security upon which to base credit. These were and are the distinctive principles of all the Raiffeisen societies in Germany and the societies patterned after them in a dozen different countries. Outside of systems of this kind, property is the main security for credit, and the man without property, no matter how honest and industrious he may be, and no matter how deserving his use of the money may be, cannot easily secure credit. The Raiffeisen system has capitalized character and by so doing has revolutionized agricultural Germany.

A description of the system as it is at present will show its outstanding features. The local parish is the unit of or-
ganization. In general each parish has a local credit association, which is a member of the General Federation of Raiffeisen societies to be described below. The farmers who desire a better means of obtaining credit, come together and form a local union, in order to get the advantage of credit based upon their combined resources. At least seven charter members are necessary, but other members may be added later if their character is good and their reputation for honesty well established. No one who is liable to injure the reputation of the society by dissipation or lack of industry, is admitted. The principle of unlimited liability insures the careful selection of members, for those already in do not wish to run any risk by admitting questionable persons to membership.

When the societies were first organized, they had no shares and no membership fee, but now they are required by law to have shares and share capital. The shares are very small, varying from $2.50 to $25. No one who deserves credit is kept out because he cannot contribute to the capital. This principle has made for success, for the man who needs credit is the man who would not be able to contribute cash towards the capital.

The society is formed on the principle of one man and one vote. The rich member stands upon the same basis as the poor man. The meetings of the society are held annually and an executive committee or "Vorstand" as it is called, is elected.
to have general charge of the business of the bank. This committee has three members. In addition, there is a general committee of from six to nine members, which has general supervisory power over the other committees, and the general affairs of the association. These committeemen and the cashier are the only officers, and only the cashier is paid. For the cashiership, the schoolmaster, the clergyman or a leading farmer, is selected. He must be able to figure simple interest and keep a set of books. He often receives as low a salary as $2 per month, and only in the very largest associations does he devote his entire time to the duties of the position. The place of business is frequently a room in the home of the cashier, or a back room in a store building. The smaller associations are open two afternoons per week, but the larger ones are open at least a portion of each day.

The cooperative bank or credit association does only a simple banking business consisting of making cash advances, giving book credit, discounting the notes of its members at the central bank in order to secure additional funds, and receiving deposits both current and time. Non-members as well as members are allowed to deposit funds with the bank. Speculation of all kinds is forbidden. When a member wishes to get a loan, either in the form of cash or in the form of book credit, he makes application to the executive committee stating the exact purpose to which the loan will be put. This use must
be some form of production. He can borrow to buy a horse or other livestock, to buy fertilizers, to build buildings or to put a fence around his farm; but he cannot borrow to take a pleasure trip or to buy a new piano for his home. He must show that the loan will be used for some purpose, which when accomplished, should give the principal back, with interest in the form of profits. If the committee is convinced that the money will be used properly, and the credit of the applicant is good for the amount desired, the loan will be granted. The business is public and every member knows who has borrowed from the association and how much has been lent. The other members begin to watch all borrowing members to see that the funds are properly used. It has been well said that, if there are 100 members in the association, each one who has borrowed from the association will have 99 detectives watching his every act. If he is unwise in the use of the funds, if he is lazy, if he spends too much time around the wine room, or in any way shows that he is untrustworthy and that the risk is poor, the officers can recall the loan by giving four weeks notice. Thus every loan is made safe: first, by careful inspection before the loan is granted; and second, by careful inspection and supervision of the use to which the loan is put. The aim has not been to make credit easy. It has rather been, to make it hard to get, but obtainable when needed. The success of the system has shown that this view of the use of credit is sound.
Most of the loans are made for long periods in the Raiffeisen unions. They are used for productive purposes, which in a rural district, would make loans for three or six months, the average time for which loans are granted in the Schultze-Delitzsch associations, entirely too short. The security is a promissory note in most cases, generally backed by one or two signatures in addition to that of the maker. In a few cases collateral is required, and a newcomer to the district is generally required to give a real estate mortgage as security. Sometimes if the borrower is well known and is considered a good risk, the money is lent to him, without security or backing other than his own signature. This is more frequently done in the case of book credit, than in cash advances, for the credit can be withdrawn at any time, if thought best. If the loan runs more than one year, it must be reduced by annual payments.

The capital, which in 1909 totalled $461,089,632 for all the associations comes from five main sources. The proportion of the total loanable capital furnished by each source is as follows:¹

<table>
<thead>
<tr>
<th>Source</th>
<th>Proportion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital</td>
<td>1.3%</td>
</tr>
<tr>
<td>Reserves</td>
<td>2.6%</td>
</tr>
<tr>
<td>Current deposits</td>
<td>9.3%</td>
</tr>
<tr>
<td>Savings deposits</td>
<td>7.3%</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>11.3%</td>
</tr>
</tbody>
</table>

An examination of the above table will show the proportion of the capital which is obtained from the shares is very small, owing to the fact that the maximum value of shares is $25.

¹ Powell's Cooperation in Agriculture, p. 280.
The main source of the loan capital is in the deposits which the above table gives as 85% of the total, over 75% being savings deposits. This would indicate that the aim of Raiffeisen is being met, for his desire was that the societies should develop habits of thrift and industry among their members. Contrasted with the terrible conditions before the introduction system of the table it shows the great value of the societies. They prevent hoarding, as well as encourage savings by the payment of interest on the deposits, the rate in general being one per cent less than the rate charged on loans. Most of the societies pay one-half per cent less on the deposits of non-members than they pay for the deposits of members. The local unions or societies desire to keep in good standing with the district branch of the great central bank of the Raiffeisen societies, the Central Agricultural Loan Bank, and hence keep a large part of their deposits on deposit with it. Only sufficient funds to meet the ordinary demands of business are kept in the vaults of the local associations. The other liabilities mentioned above consist largely of notes rediscounted at the central or district bank.

The object of these societies is not financial gain, but the social, industrial and moral betterment of the community. For this reason, the dividend rate is limited to the rate charged for loans. Because of the small shares and the fact
that each member owns but one, the dividends are only large enough to cover the cost of a subscription to the periodical of the General Raiffeisen societies, and are so used. The remainder of the profits, if any, goes into three funds. Any loss which may have occurred during the year, by the failure of a borrower to repay a loan, or for any other reason, is paid from the profits. One fifth of the remainder goes to some form of social betterment work in the community of the union, and the remaining four-fifths goes to the reserve fund. Profits are made possible because of the fact that the funds are lent at a higher rate than it costs to obtain them, either by payment of interest on deposits or by rediscount.

The reserve fund is divided into two separate funds. The first of these funds is used to cover all losses, if any, which have not been paid from the profits of the union. The other fund constitutes the real reserve of the union, but it is used as loanable capital. Should it become too great for that purpose, it would be used for some form of public work which would benefit the entire community. If the society should disband, the reserve would not be distributed among the members, but would be held in trust until some other cooperative society was formed in the parish and it would then be given to them.

This provision was adopted to prevent dissolution of the society for the sake of sharing in the distribution of the reserve.
The main function of the credit unions is the granting of credit to their members, but many of them aid in carrying on cooperative production, such as dairies, granaries, vineyards, and elevators. One important function is the purchase by the association of blooded stock and expensive machinery for the common use of the members. In certain sections they help deserving members to acquire farms by purchasing the land and taking a first mortgage as security. The member then pays for the farm by small annual installments. However, this is not a common practice because the mortgage associations can do that work better than can the credit unions.

A central bank is an essential part of the Raiffeisen system, because it has certain definite functions to fulfill. One of the chief of these, is the equalization of funds between banks having a surplus and those needing funds to meet the demand for loans. It is able to do this efficiently, and thus aids in keeping all the deposits lent out at interest. Another function is the granting of credit to newly formed local unions or banks until they can obtain deposits to meet the demand for loans. It can do this safely because it has the combined unlimited liability of all the members of the new association, and as care has been taken in the selection of all the members, the unions are safe. The third and possibly most important function of the central bank is the discounting of notes and other forms of commercial paper for the local associations. It dis-
counts all notes which are presented by the local unions, after having been indorsed by them through their officers. In this way all the resources of the local association are added to those of the maker of the note and his indorser, and the note becomes eligible for rediscount.

The central bank of the Raiffeisen unions, the Central Agricultural Loan Bank, is organized as a joint stock company. The stock is held by the local unions. The central bank is located in Berlin, but it has thirteen branches, located in the principle cities of the empire. The local banks deal with the central bank through these branches. In 1908 the amount of business done by the bank totalled $180,000,000, which, however, did not represent the total business carried on between the local banks, as many of them did business directly with each other, without the intervention of the central bank. The capital of the central bank, in 1908, was $2,149,000 which was held by 4,372 local associations. Its strength is shown by the fact that instead of being in debt to the commercial banks, it had a cash balance of $750,000 with them.

Each local society, besides being a shareholder in the central bank, is a member of the General Federation of Raiffeisen Societies, which has a membership of 5,047 cooperative societies of different types. Of these, 4,340 were credit unions and 707 were producers societies of different kinds.

1 Herrick's Rural Credits, p. 291.
2 Wolf's Peoples Banks, p. 143.
3 Wolf's Peoples Banks, p. 143.
4 Wolf's Peoples Banks, p. 146.
These societies or unions had deposits in 1909, amounting to approximately $100,000,000 and their outstanding loans totalled $93,433,250. The average deposit was $370, the average loan was $150, and the average membership of the locals was 95.

Ralph Metcalf, a member of the American Committee, in an address at Spokane, Washington, 1914, said, "The Raiffeisen system has taught that 10 times nothing is something and that 100 times nothing is $100,000." This is only a way of stating the fundamental principle of the system, that of cooperative credit. The intangible credit of the individual is worthless under our present system, but in cooperation it becomes tangible and the combined credit of 100 members will allow the association to borrow at least $100,000. This idea, combined with the principle of the unlimited liability of the members of the association for its debts, has been largely responsible for the success of the unions. Another wise provision is the limitation of the territory of the unions to that of one parish. This has made possible the careful selection of members and the direct supervision of loans. Still another wise provision is found in the fact that there is only one salaried officer, the cashier. This has removed the struggle for office, and its resulting evils. It carries out the idea that members should give what they have time and credit for that which they have not — money. Another element of success was the prohibition of profits and the non-division of the reserve in case of dissolution of the union. Speculation is forbidden, and as the business of the association

1 Wollf's Peoples' Banks, p. 147.
2 Herrick's Preliminary Report to President Taft, p. 15.
 consists only of simple discounts, loans and deposits, there is no chance for it to fail. These are but a few of the many elements which have made the unions such a remarkable success.

Section 2

The Schulze-Delitzsch Credit Associations

Second only in importance to the Raiffeisen system of village banks in the field of short time credit in Germany, is the Schulze-Delitzsch system of credit associations, which do for the urban resident, what the Raiffeisen unions do for the dweller in the country village. They were founded by Dr. Schulze and his friend Dr. Bernhardi about 1850 and first took the form of associations for the purchase of raw materials for the carpenters of Delitzsch and for the shoemakers of Eilenburg (the residence of Dr. Bernhardi). These two men were impressed by the hardships of the poorer classes and determined to do for them what Dr. Raiffeisen had done and was doing for the farmer of his community.

It is unnecessary to describe the Schulze-Delitzsch system in detail as it is much like the Raiffeisen system. Possibly the main difference in the two types is found in the different field of work. The Raiffeisen system has nearly all its unions in the small villages, and 88% of its loans go to the farmers. The following table giving the membership of the Schulze-Delitzsch associations by occupations shows that
most of its members live in the towns and cities.

Membership of the Schulze-Delitzsch Associations.¹

<table>
<thead>
<tr>
<th>Category</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent farmers</td>
<td>27.2%</td>
</tr>
<tr>
<td>Hand workers</td>
<td>24.06%</td>
</tr>
<tr>
<td>Merchants</td>
<td>9.95%</td>
</tr>
<tr>
<td>Wage earners</td>
<td>13.47%</td>
</tr>
<tr>
<td>Doctors and druggists</td>
<td>7.32%</td>
</tr>
<tr>
<td>Retired persons</td>
<td>8.21%</td>
</tr>
</tbody>
</table>

The Raiffeisen system, being organized for the benefit of agriculturists, found it necessary to extend credit for from three months to ten years, but as the Schulze-Delitzsch system lends to classes which can get returns more quickly from the investment, most of its loans are made for three months, subject to renewal if approved by the credit committee of the association.

The methods of the organization and the officers are nearly the same as in the Raiffeisen system except that the Schulze-Delitzsch unions have a special committee whose duty it is to determine the amount of credit to which each member is entitled. This is done by the examination of his property and the consideration of his past record and reputation. A record of the amount of credit granted each member is kept, and then when application is made for credit, the executive committee uses this record in determining whether or not to grant the application. The executive committee as well as the cashier are paid, for Dr. Schulze believed that "The laborer is worthy of his hire".

¹ C. R. Fay's Cooperation at Home and Abroad, p. 42.
Schulze believed firmly in a large amount of share capital and large shares. For this reason the shares in his associations have a par value of $75 rather than from $2.50 to $25.00 as in the Raiffeisen unions. Hence the share capital is a comparatively large part of the total loanable capital, as is shown by the following table.\(^1\)

<table>
<thead>
<tr>
<th>Share capital</th>
<th>14.87%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reserves</td>
<td>6.43%</td>
</tr>
<tr>
<td>Deposits and Rediscounts</td>
<td>78.7%</td>
</tr>
</tbody>
</table>

The object is to build up a large permanent capital contributed by the members themselves. This will encourage saving by the members and will reduce the dependence upon deposits and rediscounts.

The capital as well as the deposits is lent to the members as in the Raiffeisen system, and like that system, the borrower must show that the loan will be used for some productive purpose. However, a careful supervision of the purpose to which it is put is lacking for its use is industrial rather than agricultural, and careful inspection of this type of private business is naturally impossible. The different ways of securing the loan and the extent to which each method is used are given by Powell for the year 1908 as follows: unsecured promissory note, 3% of the loans; personal pledge, 77%; collateral security, 20%. Included in the term, personal pledge, as used above are many

\(^1\) Powell's Co\_operation in Agriculture, p. 290.
bills drawn by an acreditor upon a debtor and after acceptance by him, discounted at the local bank or credit association. Real estate mortgages are not accepted as security, for experience has taught that they are not satisfactory for a bank of this type, as they are not fluid enough to meet sudden demands for currency.

Many of the loans are made in the form of book credit, and as Germany develops the use of the check, this form of credit will increase. A special characteristic of this system is that they charge interest on only the amount of the actual debit balance rather than the total amount of credit extended. If there is a credit instead of a debit balance, interest is paid on the average amount of the balance.

A percentage of the profits is divided in the form of dividends, but most of the profits go to the reserves, as a large dividend would tend to commercialize the institution and thus defeat its object. Some have argued that in all cooperative credit institutions the rate of interest should be lowered rather than allowing profits to pile up in the form of reserves. Schulze-Delitzsch showed the soundness of his views by declaring that cheap credit is dangerous and that the interest rate should never be brought below 4%.

Another vital difference in the two systems is that unlike the Raiffeisen system, the liability of members for each others
debts is limited in about 40% of the associations, to four or six times the value of the shares held. Greater credit can be secured by the unlimited liability societies, but many have felt that in the cities the members cannot know each other as well as in the country; nor can they keep as close a watch on each other's business. Because of this they have limited their individual liability. Schultze differed from Raiffeisen in advocating large districts and the representation of various classes in the membership. He felt that the more members there were, the safer the bank would be and that if different occupations were represented, the savings and consequently the deposits would be more evenly distributed throughout the year. It is probable that each adopted the plan best suited to the class of members with which they were dealing. As Schulze did not supervise the use of the loan and depended upon actual resources rather than upon character as a basis for granting loans, the idea worked successfully in his associations where it would not have been so successful in the Raiffeisen unions.

Unlike the Raiffeisen unions, the Schulze-Delitzsch associations do not have a great central bank, but do their clearing through the Dresden and other commercial banks, with which they have special arrangements. As these banks are located at a considerable distance from some of these associations, those

1 Powell's Cooperation in Agriculture, p. 91.
most remote have experienced considerable difficulty in getting the credit to which they felt they were entitled. This difficulty has been solved in two districts by the organization of district banks, the stock of which is held by the local associations. These district banks receive deposits from and discount notes for the local banks and act as their agent in dealing with the large commercial banks.

The success of the system is shown by the following figures covering the year 1908. There were approximately 1000 local associations having a membership of over 600,000 and a capital of $75,000,000. Their deposits totalled $250,000,000 and the turnover for that year was $925,000,000. Comparison of these figures with those given for the Raiffeisen unions shows that this system does business on a much larger scale, because its clients are those who need much larger loans than do those of the Raiffeisen system.

Both systems have been a success and both have realized to a large extent, the aim of their founders -- the moral, social and financial betterment of the classes among which they were formed. Both have many features which the farmers of the United States could adopt with profit. We must study these pioneer efforts in the field of rural credits, if we would successfully solve the needs of our rural districts.

1 Powell's Cooperation in Agriculture, pp. 290, 291.
The demand for short time credits in Germany is met by the "Banche Populari", or people's banks, and the "casse rurali" or credit unions. The former are organized on the model of the Schulze-Delitzsch associations in Germany and the latter are patterned after the Raiffeisen system of credit unions.

In 1913 there were 83 of the Banche Populari scattered throughout Italy. They were organized to meet the demand of the so-called middle "classes" for short time credit for industrial uses. A bank can be organized in any community by those interested coming together and raising the necessary capital, which is done by the subscription of shares worth from $5 to $10. A large board of directors is elected and an executive committee of the directors is chosen to conduct the affairs of the bank. The executive committee prepares a list of the members and determines to what amount credit can be granted to each. Using the list as a guide loans are granted to the members upon application. The loans can be guaranteed either by personal security, i.e., character, the indorsement of one or more securities, by collateral, or by acceptance, real or accommodation. The loans are made for a short a time as possible, preferably for three months and are kept as small as possible for the associations believe that a
wide distribution of their funds makes for security.

Funds are obtained by both current and long time deposits, by rediscount of paper at one of the commercial banks, and by the use of the capital and reserves of the association. A few of the banks also issue long time interest bearing bonds secured by the general property of the banks, but this is not a common practice for it requires payment of interest of funds for which they have no use at certain times of the year. The object of the banks is to provide a method whereby deserving artisans, farmers and merchants, may secure funds for the conduct of their business. Their collective assets and the individual honesty of the members are used as security for the loans. Like similar systems in Europe the Banche Popolari system of associations has proved to be very successful, and has greatly benefited the classes for which it is intended. In 1907, there were 832 banks having a paid up capital of over $18,000,000 and loans totalling about $100,000,000. The average membership of the local associations is about 642.¹

The "cassi rurali" or rural cooperative societies correspond roughly to the Raiffeisen unions of Germany. They have been formed largely or entirely among the farmers of Italy and are unique in that they have little or no initial capital, but build up a reserve fund through the payment of a small initiation

¹ Wollf's People's Banks, p. 291.
or membership fee. The funds from which loans are made are obtained from the deposits of members and also from outsiders who deposit with the bank. Loans are of two kinds, those under two years and those running from two to ten years. The latter generally have to pay a higher rate of interest, but are repayable by installments.

Although the system started under difficulties, it has now reached a point where it can be and is being a great help in bettering the economic and industrial condition of the Italian peasants. Because of the fact that these unions have no central organization, it is hard to get reliable statistics, but we know that on December 31, 1913, there were 2904 of the local unions. Two-thirds of these unions were composed exclusively of Catholics, and these unions combined cooperative buying with their credit functions. The capital and reserves of these locals amounted to $600,000 and they had deposits totalling $20,000,000. Their loans are for short periods and hence they were able to lend $50,000,000 during 1913.

1 Herrick's Rural Credits, p. 359.
2 Herrick's Rural Credits, p. 358.
III

SOME EXAMPLES OF AMERICAN ATTEMPTS TO PROVIDE BETTER RURAL CREDIT FACILITIES

Section 1

The Canadian System of People's Banks

In the search for successful systems of people's banks or rural cooperative credit unions, Americans have gone to Europe and have based their conclusions on the success or failure of the systems established there, without regard to the history and plan of successful systems already in operation in America. Prominent among American systems is the type of credit unions or people's banks in Canada, patterned after the bank established at Levis, Quebec, in 1900 by M. Alphonse Des Jardins. M. Des Jardins, who was a well to do citizen of Levis and a member of the Canadian Parliament from his district, was greatly interested in the welfare of his fellow citizens and had been studying for some time the systems of credit unions in Europe founded by Raiffeisen and Schulze. He realized that the people of his district were greatly handicapped by lack of sufficient money to carry on the ordinary processes of production in an efficient manner. It was evident that more money was needed by both the urban and rural classes, but it could only be obtained from the usurers who charged an exorbitant and
ruinous rate of interest. The citizens were honest and industrious, but lacked the definite material security required by the stock banks of the province before a loan would be made. M. Des Jardins felt that could the European systems of cooperative credit be adapted to the conditions prevailing in his province, they would provide the means whereby the farmers and artisans of the district could obtain needed funds.

Accordingly in September, 1900, he called some of his friends together and proposed to them that they form a credit union along the lines that he suggested. They readily agreed to his suggestion and appointed a committee to draw up a constitution and solicit for shares of the capital stock. A public meeting was held on December 6th, 1900, which was attended by 50 of the most intelligent citizens of Levis and the surrounding country, and the bank was organized. It was to operate in the town of Levis, a place of about 7000 population, situated across the river from Quebec, and composed of railroad men, factory hands, artisans and small merchants. In order to test the operation of the system among farmers as well as townspeople, two parishes immediately tributary to the town and formerly a part of it, were included in the territory of the union. Thus it had both urban and rural members, a fact which served to give it a severe trial.

In establishing this bank, M. Des Jardins did not adopt

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outright any one of the systems in use in Europe, but rather took the principles from each which he thought were suited to American conditions, and combined them into a system which is quite radically different than any before known. Experience has shown the wisdom of this act.

The plan as adopted by the bank at Levis, and the one which has been a model for subsequent unions in both the United States and Canada, provides that any honest, industrious resident of the territory in which the union operates, may become a member by buying one share of stock at $5. This can be paid for by 50 weekly payments of $.10 each if desired. The number of shares held by each member cannot be greater than 600, but there is no limitation of the number of members in the districts. The districts are limited to the territory included in a parish, a ward, or an election district. The money raised by the sale of shares together with the deposits of the members, constitutes the working capital of the bank. Either shares or deposits may be withdrawn at will, the distinction between them being, according to M. Des Jardins, that "the shares are supposed to be made up of the members savings, with a view to meeting future contingencies more or less remote; while the deposits are put aside for almost daily use". The shares correspond roughly to time deposits while the deposits resemble the ordinary checking account in a commercial bank. In inaugurating this

system of a withdrawable capital he was but following the example of the uncapitalized savings banks of the New England states which depend wholly upon deposits for a working capital. Although new, this phase of the plan seems to have been a success, at least among the type of people with which he was working.

The funds so raised are administered by two committees chosen by the shareholders at their annual meeting. The first committee is the board of administration, composed of from 5 to 9 members, which has many powers of supervision and control over the society and its business. Among its powers are the right of electing the manager and other officials; the right to admit or expel members; the right to recommend to the annual meeting the plan to be adopted for disposing of the profits of the year; and in general all the powers not given to the other committees.

The credit committee is composed of three members and supervises the granting of loans to members. It makes general rules in regard to the loans; regarding the security to be required; purpose for which loans shall be made; rate of interest, etc. All applications for loans must be approved by this committee by an unanimous vote. It observes the following principles in granting loans. The borrower must state the specific purpose to which the loan will be put. This must be some productive or economical use. If the use to which the funds of the society are to be put by the borrower is improvident, the
committee will refuse to grant the loan, no matter how good the security offered may be, for the chief purpose of the society is to encourage thrift. Loans are granted only to members and are for terms varying from a few months to 15 years. They are repayable by annual or semi-annual installments, the committee and the borrower fixing the terms by mutual agreement. This agreement must be carried out absolutely by both parties. The moral character of the borrower is the only security required in most cases, but indorsements may be required by the committee, if they think best. It is worthy of note, in this connection, that in the 14 years that the Levis society has been in operation, not one cent has been lost through the failure to repay a loan.

Because the capital is withdrawable, the reserve funds of the association become in fact the non-withdrawable capital. These funds are two in number. The reserve fund is made up of all profits after a dividend of 7% has been paid to stockholders. In addition to this fund, there is the "providence fund" which is composed of a tax of 10% of all annual profits, until the fund so accumulated equals one half the average annual dividends paid to stockholders. Thus there are two funds designed to meet any concerted withdrawal of the capital stock by the shareholders. A part of this fund equal to from 12% of the total is kept as a reserve in the vaults of the local union,
but the remainder is lent out on the same basis as the capital stock and the deposits.

The policy of the society has always been to place emphasis on the encouragement of industry and thrift, rather than upon the making of a large profit. In this they have been very successful, for as M. Des Jardins has well said, "Unlike the ordinary savings bank they have not a mere slot in their wall through which to receive money, but a mouth wherewith to give advice and a heart wherewith to feel. In their keeping, depositors, or members, so to speak, see their money, see it safely held, see it laid out profitably in the locality, benefitting the district, and producing more money, whereas else where it disappears to go, no man rightly knows where, to the great money markets." This advantage combined with the fact that they know that the bank is controlled by their own members whom they have helped to choose, has won the confidence of the people and it seems that the system is to be a permanent success.

The parent bank at Levis after an existence of 9 years, in 1909, had over 1000 members; its assets were $102,870.35 and in that year it lent $110,404.47 to 638 different members. By 1913 its assets had increased to $266,385.03 and its loans were proportionately large. The success of this bank was so pronounced that after 1903 the movement spread rapidly and by the end of 1913, there were 141 credit unions in Quebec and Ontario,

1 Mitchell's *People's Banks in North America*, p. 20.
and in addition there were 39 unions patterned after them in Massachusetts, and one in New Hampshire.¹

M. Des Jardins seems to have inaugurated a system which is adapted to the needs of the industrial communities of eastern Canada and the New England states and one which will furnish at least suggestions, if not a model, for the extention of some similar system to all parts of the United States.

Section 2

Credit Unions in Massachusetts

Although credit unions as described above had been organized for many years, both in Europe and in Canada, it was not until 1909 that the first state legislature authorized their formation in the United States. In that year, the legislature of Massachusetts passed a law authorizing the formation of credit unions based partly on the system introduced in Canada in 1900 by M. Alphonse Des Jardins, and partly on the cooperative banking system already in operation in the state of Massachusetts.

The law provides that seven citizens desiring to organize a credit union may apply to the state Bank Commissioner at Boston for a charter. This official then advertises a date on which he will hold a public hearing in the town which is to be the head quarters of the union. The interested parties then appear before him and show that such an organization is necessary and

¹ Mitchell's People's Banks in North America, p. 30.
will be likely to succeed.

If he is convinced of the need for, and the probable success of the union, he recommends to the Commissioner of Corporations that he issue a charter. After this is obtained other members are admitted and the organization is completed by the members in their general meeting.

Membership is restricted to residents of the territory of the union and each applicant accepted for membership is thought to be an industrious and honest citizen to whom it would be safe to loan a portion of the funds of the union. Members must buy at least one share at $5, which can be paid for at once or in installments as the subscriber decides.

A board of directors of not less than five members having the general direction of the policies of the union, is elected. A credit committee of not less than 3 members is also chosen by the shareholders, as is also a supervisory committee of 3 members which has general powers and acts as a board of audit. A manager and clerks are appointed by the board of directors. All except the latter officers serve without compensation.

Loans are made to shareholders only, for short or long periods as desired, and in general are secured only by the moral character of the borrower. The credit committee has entire charge of the granting of these loans and will lend only for productive purposes. Funds are provided by the paid in capital and by the savings of the members, deposited in the bank.
Should the demand for loans not equal the supply of funds, the surplus may be deposited in any bank doing business in the state.

In order to provide against any possible loss, a guarantee fund is provided by setting apart 20\% of the profits each year until the fund equals the total paid in capital. This fund is invested under the supervision of the directors.

Since the law was passed, 51 unions have been organized under its provisions, and of this number 46 were in operation on October 31, 1914. These 46 unions had a total membership of 6,149, and had made loans totalling $371,353.47 during the year ending October 31, 1914. Their total assets were $379,358.23, and they had paid in dividends, $8,335.80 during the year. The loans had varied from $5 to $1,000 and had been made for periods varying from one week to one year, and an occasional loan on real estate for an even longer period. The rate of interest charged varied from 6\% to 12\% depending on the security offered and the time for which the money is loaned.\(^1\)

Section 3

Credit Unions in New York\(^2\)

On the 16th of April, 1914, the legislature passed an act providing for the establishment of credit unions in the state

\(^1\) I am indebted to Mr. W. J. Stanton, General Manager of the Massachusetts Credit Union, 78 Devonshire St., Boston, for the above information.

\(^2\) Laws of New York, Ch. 369, Article 11.
of New York. The plan adopted is modelled after the Massachusetts plan discussed above, and does not differ from it in any of its essential features.

A letter from Mr. E. L. Richards, Superintendent of Banking for the state of New York states that under this law, a number of unions have already been organized and that others are being formed. The unions organized by the Jewish Industrial and Agricultural Aid Society are changing their form of organization, where necessary, to comply with the law, and are arranging to make use of its provisions in enabling them to do the business which they had previously been doing without the sanction of the law. As the date for the first annual report of these unions has not yet arrived, it is impossible to give any facts regarding the business which they are doing.

Section 4

Credit Unions in Wisconsin

Wisconsin added a section to her banking laws in 1913, which provides for the organization of credit unions under the authority of the state banking department, and provides for their inspection and control by the state Commissioner of Banking. The law is modelled after the laws in force in Massachusetts and New York, and contains no distinctive features. A letter from the Commissioner of Banking states that as yet, (March, 1915) no unions

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1 State Banking Laws of Wisconsin, Revision of 1913, pp. 67-73.
have been organized under its provisions.

Section 5
Credit Unions in Texas

On July 1st, 1913, a law went into effect in Texas providing for the organization of credit unions. It was modelled after the Massachusetts law, the chief changes being that ten rather than seven members are necessary before the union can receive its charter and that the capital stock is divided into shares of $25 instead of $5. The State Banking Commissioner states that up to February 1st, 1915, no unions have been organized under its provisions.

Section 6
Building and Loan Associations in the United States

Perhaps the most successful form of credit cooperation in the United States is found in that class of societies known as Building and Loan Associations. Starting in Philadelphia, Pennsylvania, in 1831, their growth has been steady; and to-day they number over 6,000 and are found in all parts of the country, and in the small town or rural district as well as in the large cities.

Building and Loan Associations can well be divided into two classes, local and national associations. The local associa-

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1 State Banking Laws of Texas, Ch. IX, Sections 232-255.
tions operate only in a restricted area, usually a certain village or township, only a few operating in as large an area as an entire county. The national associations, as their name indicates, are not limited to a certain area but operate in all parts of the country. This latter class are, however, few in number as compared with the local associations. Their success has been limited because of the added expense of operating branch offices or associations; the expense of hiring officers who devote their entire time to the work; and because of the fact that they are not able to judge of the character and industry of proposed members as well as can the officers of the local associations who know every member of the community. Another difficulty is that the national associations cannot accurately estimate the value of the property upon which a loan is desired because of the lack of knowledge of local property values, nor can they carefully supervise the use of the loan. Because of these facts it seems to be granted that the local association is the more successful type.

The object of all the different types of these associations is, "to encourage industry, frugality, home building and saving among its members; the accumulation of savings; the loaning of such accumulations to its members; and the repayment to each member of his savings when they have accumulated to a certain sum, or at any time when he shall desire the same, or
the association shall desire to repay the same."

An illustration of how the associations operate will perhaps make clearer the means by which the above objects have been accomplished. We will suppose that one hundred men live in the same town or community and each one desires to accumulate his savings so that he may build or purchase a home. Each of these men is able to save at least $1 per month, but that amount will not enable him to secure the home unless he can cooperate with some of his neighbors who have like desires. In order to accomplish this, a corporation is formed, each member of which holds at least one share. On each share $1 must be paid each month as dues until a certain set amount is reached, usually $100 or $200. If each of these 100 members has one share, it follows that $100 will be paid into the treasury each month. As soon as these savings accumulate to a sufficient sum they are lent on good security, generally to one of the members of the association who uses the loan for the purpose of building a home. Among the one hundred members, there would undoubtedly be several members who would desire to borrow the accumulated funds, and various methods were adopted in the older associations to determine which one should have the privilege. Generally the member who was willing to pay the highest premium in addition to the ruling rate of interest, secured the loan. This difficulty has been avoided in some of the newer associations as
will be described below. The borrower must give to the association, a first mortgage on the property purchased and must at the same time subscribe for enough shares so that their value at maturity will be at least equal to the amount of the loan. Thus the association has two sources of profit, the premium paid for the loan and the interest on the loan. These profits are divided proportionately among the share holders, and are applied to reduce the time necessary for the shares to reach their maturing value. Finally, it is found that the dues paid in, combined with the profits which have been added, equal the value of the share, which is generally $200. The business of the association is then terminated, the shareholders who have not been borrowers receiving their cancelled notes and mortgage. Should the amount borrowed be less than the matured value of the share, they receive the difference in cash.

This is in brief the method of operation of the simple terminating associations. It shows the principles upon which the associations are founded, but a plan as simple as the above has many defects. One of the chief of these is that the association is required to go out of business when the shares have matured. Another is that there is but one series of shares. If a member or some one wished to join the association after it had been organized for some time, and become a borrower, he would be required to pay an amount in back dues equal to the amount that
had been paid in by each of the original members, for all members were required to be on the same basis. Another defect was that funds could be lent only to members, and if the members did not wish to borrow all the funds available, the funds must either lie idle or the members be forced to borrow. This latter plan was adopted, but it was not satisfactory.

To overcome these difficulties, the serial plan of issuing shares was adopted. This provides for the issue of shares at least once a year, thus providing for the perpetual existence of the association as well as doing away with the requirement that new members must pay back dues. Thus a member could join at any time and pay only his annual or monthly dues. It also has to a large extent done away with the third defect mentioned above, for it provides for the entrance of new members at any time, and these new members will be, to a large extent, borrowers because in most cases they have joined the association for that purpose.

The membership of the building and loan associations is divided into two classes, borrowers and non-borrowers, the latter class joining solely for the purpose of having a safe place in which to invest their savings. In 1893 only about 30% of the members were borrowers. The borrowers are again divided into two classes, those who borrow on real estate security and those who borrow and give their stock in the association as security.
Loans are nearly always confined to the membership of the association making the loan. In most associations the loan may be terminated at any time by a payment equal to the difference between what has been paid in plus all accumulated profits, and the value of the shares at maturity.

The management of the Building and Loan Association is generally vested in a board of directors, composed of the president of the association, the treasurer, secretary and attorney and a certain number of members in addition. Upon the way in which this board and the officers discharge their duty, depends the success of the association, for they must decide the policies upon which the association will be conducted, and must exercise great care in placing the loans. These officers generally serve for a very nominal salary for in only a very few associations do their duties require any large part of their time.

The benefit of these associations both to their members and to the community in general is great. Aside from the financial advantages which the share holders obtain, the value to the community of having a class of permanent home-owning citizens, which these associations make possible, cannot well be over emphasized. The home-owner acquires a tangible interest in the welfare of the community. He rises, both in his own estimation and in the estimation of the community and that fact makes for thrift and responsibility. That these associations do enable working men to acquire homes is shown by the investigation of the Department
of Labor. They found that 4,444 associations were the means through which 314,755 homes were secured, and in addition that 28,458 other buildings such as lodge halls and churches were acquired by members of these same associations. About 60% of these homes were acquired by working people, and 30% of them were acquired by such classes as foremen in factories, tradesmen, small merchants and professional men, etc.¹

Recent figures as to the success of building and loan associations seem to be difficult to secure. There is an organization known as The National Association of Building and Loan Societies, which is supposed to hold annual gatherings, but as far as can be determined, they have not met since 1911. In that year they found that there were 6,113² associations in the United States having a membership of 2,355,068 persons. In that year there were in Iowa, 49 associations having a membership of 16,500. For some reason the Iowa associations seem to have decreased in number since 1901 when there were 82 associations. The competition of an efficient system of saving banks combined with many opportunities for profitable investment has perhaps been responsible for the decrease in the number of associations in Iowa.

The relation of the building and loan associations to the general subject of coöperative credit unions is easily seen, for they are but specialized forms of credit associations. With few

exceptions, there have been no other forms of such associations, or unions introduced in this country, and our experience with this particular type of union will be of use in the establishment of unions covering a broader field. Our experience with the building and loan associations has probably shown, as indicated above, that the field of operation of any credit union should be confined to a small area. This conclusion is also reinforced by the experience of Germany and other countries where credit unions are in operation. On the whole, it can be said that the success of the building and loan associations has been so great that it would argue for the success of the credit union, organized on the same lines and hedged about by the same restrictions.

The recent action of the state legislature of New York, in establishing the Land Bank of the State of New York, shows another use of the building and loan association. This land bank is to be based on the building and loan associations already in operation in the state, and simply unites them for additional functions.

Section 7

The Jewish Agricultural and Industrial Aid Societies

The beginning of Jewish immigration to America goes back to an early date, and their industrial activities date back to colonial times. However, it was not until the year following the Russian persecutions of 1889, that the coming of Jewish agricultural immigrants from that country began to assume large
proportions. It was evident that these farmers would need financial assistance, and upon the request of Oscar S. Strauss in 1891, Baron de Hirsch, who had greatly aided the Jews in Russia, founded a special fund of $2,400,000, the income of which was to be applied to the aid of Jews in America. While the encouragement of agriculture was its chief aim, it was to aid the immigrant in every field.

It was soon seen that a separate organization would be needed to take charge of the agricultural uplift work of the foundation, so in 1900, the Jewish Agricultural and Industrial Aid Society was formed for that purpose. Its main work has been the making of loans obtained partly from the Baron de Hirsch funds and partly from the Jewish Colonization Association. The loans are made to Jewish farmers to enable them to buy farms or for the improvement of farms already owned. It lends at 4% and takes a mortgage or collateral as security. In the year 1913, the society made loans totalling $244,977.85 to 423 farmers in 21 different states.

However important and helpful this phase of the work of the society may be, it is its credit unions that we wish to notice most particularly in this study. The society early recognized the need for short time personal credit and as early as 1907 considered the introduction of a system of credit unions.

1 Agricultural Activities of the Jews in America, p. 51, by Robinson.

2 Report of the Jewish Agricultural and Industrial Aid Society for 1913, p. 51.
based on those in use in Europe. However, it was not until 1911 that the first union was organized, for the farmers had to be informed of the advantages to be gained from such an organization. In that year three were organized; five were formed in 1912; and nine in 1913, making a total of seventeen local credit societies. Eight of these are in New York, five in New Jersey and four in Connecticut. One has been formed in Massachusetts, but it is incorporated under the credit union law of that state.

These local unions are organized on the model of the Raiffeisen societies of Germany. A union can be formed in any community in which at least 20 Jewish farmers can be found who are willing to unite to form the union. Each member buys one or more shares of stock at $5 per share, and when $500 has been raised in this way the Jewish Agricultural and Industrial Aid Society lends the union $1,000 at 2% interest. Thus they have a loanable capital of $1,500. The union is governed by a general assembly of the stockholders which determines matters of general policy and is the final court of authority. The President, Vice-President, Secretary and Treasurer form the credit committee to which applications for loans are made. It will be remembered that the society lends long time loans in large amounts direct to the farmers, so we can expect that these unions will occupy a different field. Loans are granted for productive purposes only for a period of not over six months.
The loan is limited to $100 and 6% interest is charged. The security for the loan is determined by the credit committee, the usual form being second or third mortgages, or collateral, or sometimes a promissory note with one or more indorsers. A moderate dividend is paid to stockholders and the remainder goes to the surplus.

On September 30, 1913, 17 of these associations had been organized with total membership of 515, giving an average membership of a little over 30 members. Their total capital and surplus was $9,165, an average of but $539.12 per union, but on this amount they had lent in the previous year $73,624.66, an amount eight times as great as their capital. The average loan was for $66.75. Their profits had netted them 13½% on the investment.

It is too soon after the inauguration of the system to say that these credit banks or unions have been or will be an unqualified success, but as far as can be seen they are founded on a sound principle and seem to be an effective adaptation to the conditions and needs of the United States of the principles governing the granting of short time personal credit in Europe. The unions have benefitted the members in every case and have been financially profitable as well. They have given their members an opportunity of freeing themselves from the usurer and loan shark and from the pernicious system of crop liens or store credits. Their future progress will be carefully watched.

1 Jewish Agricultural and Industrial Aid Society, Annual Report for 1913, pp. 29-30.
and they will have at least shown that such a credit union can be operated on American soil.

Section 8

Land Mortgage Associations in Wisconsin

In the year 1913, Wisconsin, besides establishing the system of credit unions discussed above, passed a law authorizing the formation of land mortgage associations in that state. The plan provided combines some of the features of the German Land-schaften systems, with certain features of the Land Bank of the State of New York, and besides adds some distinctive provisions not hitherto used in any similar system.

The plan as adopted provides that any fifteen adult resident freeholders may combine to form a local land mortgage association. They can proceed to form a temporary organization and subscribe the capital, which must be at least $10,000. After the preliminary organization is approved by the State Commissioner of Banking a charter is issued and permanent officers are elected. Besides the usual officers, president, vice-president, secretary and treasurer, they choose a board of trustees who have general control of the business of the association, and a committee on loans.

As thus organized, the association is ready to make loans. As mentioned above, the capital stock must be at least $10,000 which gives the association funds to lend until other funds can

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1 See Section 4.
be obtained by the sale of bonds. An applicant for a loan must make a written application to the committee on loans, stating the amount which he wishes to borrow and the property which can be mortgaged to secure the loan. He must also have his property appraised by two resident freeholders, and must in addition secure a certificate from the assessor of incomes that the appraised value does not exceed the true market value of the property. If satisfied that the loan is desired for a productive purpose, and that the title is clear, the credit committee can then grant the loan. This loan must, however, be limited to not over 65% of the appraised value of the property, if improved, and 40% if unimproved. A first mortgage is taken as security. All mortgages must be subject to amortization, at least one per cent of the loan being repaid each year.

The total amount of the loan can be repaid at any time by giving six months notice, or any amount desired may be repaid at any interest paying date. If the property is sold at any time before the loan is amortized, the purchaser assumes the obligation of the mortgage.

Each local association has the privilege of issuing bonds in such amounts, for such times and bearing such rates of interest, as the board of trustees see fit. These bonds must be secured by depositing mortgages with the state treasurer equal in amount to the bonds issued. Thus all bonds issued are secured by first mortgages on real estate. These bonds can be
allowed to run until due or may be redeemed at any time by giving personal notice to the holder of the bond as shown by the bond register of the association.

Thus each local association is a unit which performs the same functions as the Land Bank of the State of New York does for the entire state, and as do the German Landschaften for an entire province. Whether this is a better plan cannot yet be determined as no associations have been organized under its provisions up to the present time (March, 1915). It would seem that one weakness of the system might be that there will be as many bond issuing bodies as there are associations and that fact would tend to confuse investors and make it difficult to determine the value of the bond as an investment. Where there is but one bond issuing body, as in New York, there will be but one kind of bonds, and thus the bonds would be more attractive to investors. However, the advantage of having the issue of bonds directly under the control of the persons who use the funds may offset the possible disadvantages suggested above.

Section 9

The Land Bank of the State of New York

New York like most of the other states of the union has for a number of years had a system of savings and loan associations, or as they are called in some states, Building and Loan

1 For the facts presented in this section, I am indebted to the Editor of the "Rural New Yorker" and to the Banking Commissioner of New York.
Associations. However, it was not until April, 1914, that the legislature of New York took the next and logical step in the development of these associations by enabling them to meet the growing needs of the farmer. The associations had up to this time required that dues or payments on shares should be paid monthly. This was all right for the city residents whose income was more or less regular, but it kept most of the farmers from becoming members, because of the irregularity of their income. Hence, the legislature gave the associations power to change their by-laws so that payments could be made quarterly, semi-annually or even annually. In addition it provided for the Land Bank of the State of New York to supplement the system of credit unions described above.¹ This bank has the power of issuing bonds to provide funds for the local savings and loan associations, which they use for meeting the demands upon them made by their new class of members, the farmers.

These local Savings and Loan Associations in New York are composed of at least fifteen members residing in one locality, and any resident being eligible to membership. Each member subscribes for one or more shares, with a face value of $100 at maturity, and pays for them in regular installments. These installments can be arranged so that the shares will mature, or be fully paid for, any time under 40 years. Regular payments are made as provided for, and at the time of maturity the value of

¹ See Section 3.
the shares can be withdrawn in cash, or used to cancel the principal of any loans that may have been made to the member.

This then is the general plan on which the Savings and Loan Associations are organized in New York, as well as in many other states. They appeal to three classes of citizens, the first of which does not wish to borrow of the association for any purpose, but wishes merely to have a safe place of deposit for its savings, and one which will pay a larger rate of interest than the average savings bank. The second class is composed of persons with a small but steady income, such as clerks, artisans, and many professional men. They take out a certain number of shares and after a few payments have been made and their reputation for honesty and thrift is established, they are allowed to borrow of the association in order to build a home, or for any productive purpose, giving a mortgage on the property purchased to the association as security. However, the amount lent is generally limited to $100 for each share owned. The borrower continues his payments on his shares and in addition pays the interest on the principal borrowed. When the shares mature, enough money will have been paid in to cancel his loan and he will have his property free of incumbrance. The third class of members is one which has just been available for these associations. It is composed of farmers who wish to borrow enough from the association to buy a farm. If the farmer has enough money to make the first payments, he is lent the remainder
needed to complete paying for the farm, as soon as he becomes a member and subscribes for shares. He gives a first mortgage on the property as security and continues his payments on the shares, which are used to cancel the debt at maturity. Should he wish at any time to make a larger payment than the regular dues, he has that right and his shares mature proportionally sooner. This method of obtaining loans will also make it possible for farmers who have mortgages from banks or other private agencies at disadvantageous terms to pay them off at maturity by securing the necessary funds from the loan association. Other farmers can become share holders and borrow money to make necessary improvements on their farms. The associations have been very successful in doing this work and the fact that there were 789 in New York, on January 1, 1915, shows that they are popular. However, their combination into a union with the Land Bank as a basis will make them more efficient and will enable them to obtain the necessary funds to meet all demands upon them, a thing which they have not always been able to do.

The act which organizes the Land Bank of the State of New York, provides that whenever at least ten of these local associations wish to unite they may do so by holding a meeting; organizing the Land Bank of the State of New York; electing officers; and applying to the Commissioner of Banking for a charter. The associations uniting to form the union must subscribe for

1 J. J. Dillon's *The Land Bank of the State of New York*, p. 12.
at least 100 shares at $1,000 each, thus making the original capital of the Land Bank at least $100,000. The local associations will pay for these shares from their accumulated surplus or from their guaranty fund. If a newly organized association wishes to become a member of the Land Bank so that it may have the right of borrowing from it, it can pay for its share from the funds borrowed, until enough dues have accumulated to pay for it. The associations may hold more than one share if desired, but must hold at least one before they can borrow from the Land Bank. When the local Savings and Loan association wishes to obtain funds from the central land bank to meet the demand upon it for loans, it simply gives mortgages held by it as security for loans to the Land Bank and obtains the needed funds. It, however, cannot pledge more than 75% of the mortgages held by it to the Land Bank, and they must all be of a type which will mature in at least 40 years from the date upon which issued.

As shown above, the Land Bank has at least $100,000 as its original capital. This can be used to provide funds to be lent and in addition it can secure funds by the sale of debenture bonds. These mortgages secured from the local association are deposited with the state Comptroller and he then authorizes the issue of bonds based on them as security. These bonds are issued for various amounts and for different periods. The bonds are sold on the open market and the funds so obtained are available for
loans to the local associations upon mortgage securities thus providing the basis of a new issue of bonds, and the repetition of the process.

A consideration of the above plan will show many good features, one of which is that it uses the local Savings and Loan associations, which are already organized and doing business in all parts of the state, as a basis and simply unites them into one strong central association or land bank, for the purpose of issuing bonds upon the mortgages held by them as security for loans. It is an economical system for it uses the local associations which have practically no paid employees, as a medium for placing its loans, and avoids a great deal of expense which could not be avoided if a separate and distinct Land Bank had been provided. Furthermore, the local associations are acquainted with land values in their localities as well as with the moral qualities of the borrower and therefore can place loans more safely than could any other type of organization. They are also enabled to watch the borrower in his use of the funds obtained from the association, and can also see that all interest payments are paid promptly as well as the payments due on the shares subscribed for. The Land Bank enables the local associations to mass all its mortgages as a basis for note issue, and through state supervision, can make them an attractive form of investment. The borrower is enabled to secure his funds at the rate the Land Bank pays on its long time bonds, plus his
proportional share of the expense of the local association. He is also given the opportunity by means of a moderate yearly or semi-yearly payment, which in most cases will not exceed the amount paid for interest alone under the ordinary mortgage system, to discharge his debt as well as pay the interest on it.

In other words, for the first time in the history of this country the mortgage on the small home or on the farm is placed on the financial basis to which its merit entitles it and on a plane equal to that of any other industrial security in the country.

Section 10

A Land Bank Under Private Control

Trust companies especially in large cities have made it a practice for several years to sell coupon bonds based upon a definite mortgage as collateral. It remained for the Woodruff Trust Company of Joliet, Illinois, to apply a new principle to trust company operations in bonds. This company through its officers made an investigation of land banks in all parts of the world and especially of the Credit Foncier of France and the Landschaften of Germany, and decided that the principles of these systems could be applied in the United States. As a result of these convictions, they established a system of mortgage bonds, the funds for which are secured by sale of bonds secured by first mortgages on real estate.

This trust company will lend money to farmers on first
mortgages up to 50% of the value of the property, giving them the opportunity of paying both principal and interest by small annual or semi-annual payments. The mortgages run for from one to thirty years, but can be paid in whole or in part at any interest paying date. To show how the plan works out in actual practice the following statements and figures are taken from the table used by the company in figuring the payments due. If the loan is for $1000, at 5% (the usual rate) and runs for thirty years, 7% of the principal each year will discharge the debt at maturity. This will mean that $35 will be paid on each semi-annual interest paying date. At the end of certain of the periods, this payment will be divided as follows:

First 6 mos. Interest On Principal Expenses & profits Amount of Principal still unpaid

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<tbody>
<tr>
<td>1st year</td>
<td>25.00</td>
<td>7.35</td>
<td>2.65</td>
<td>$992.65</td>
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<tr>
<td>3rd year</td>
<td>24.31</td>
<td>7.54</td>
<td>2.65</td>
<td>985.11</td>
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<tr>
<td>5th year</td>
<td>24.03</td>
<td>8.32</td>
<td>2.65</td>
<td>954.03</td>
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<td>10th year</td>
<td>23.16</td>
<td>9.19</td>
<td>2.65</td>
<td>908.31</td>
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<tr>
<td>15th year</td>
<td>20.59</td>
<td>11.76</td>
<td>2.65</td>
<td>812.15</td>
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<tr>
<td>20th year</td>
<td>17.30</td>
<td>15.05</td>
<td>2.65</td>
<td>677.14</td>
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<tr>
<td>25th year</td>
<td>13.09</td>
<td>19.26</td>
<td>2.65</td>
<td>504.32</td>
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<tr>
<td>30th year</td>
<td>7.69</td>
<td>24.66</td>
<td>2.65</td>
<td>383.12</td>
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<td>.79</td>
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Thus in the thirty years the borrower will have paid $2100, of which $1000 went to repay the principal, $941 was interest and the remainder, $159, the company received to cover expenses and as profits. If the money had been borrowed in the method now common, the borrower would have paid $2500 in the thirty years, and besides that would have had a large amount commissions, abstract fees, etc., to pay, because the mortgage would have had.
to be renewed frequently, and each time would have caused additional expense. As indicated above, the borrower could have paid in any amount he wished to on any interest paying date, in addition to the regular amount due. The amount paid in would have reduced the amount of principal still unpaid, and so would reduce the proportion of the regular payments going to interest and increased the proportion going to the reduction of the principal. The borrower not only saves nearly $500, but is spared the trouble of renewing the mortgage and in addition he knows that his farm can never be taken from him by foreclosing the mortgage, as his payments only amount to 1 ½% of the value of the farm at the greatest, and that much, the farm will be sure to produce.

The trust company deposits the mortgages with the First Trust and Savings Bank of Chicago, which acts as a trustee or holding company holding these mortgages as collateral for the bonds issued on the mortgages. These bonds are secured by the whole mass of mortgages held by the company, and not by one particular mortgage, so that their value does rest upon the value of one particular piece of property. To prevent an over issue of bonds the holding company must sign each bond before it can be placed on the market and must certify that it is backed by good and sufficient security. Each mortgage must involve amortization and for this reason the security back of each of the mortgages is constantly growing larger through the reduction
of the loan on the property. This principle, amortization, has enabled foreign land banks to do an immense volume of business with little or no less, because of the constant increase in the value of the securities. It seems to be just as sound and just as applicable to American conditions.

The bonds issued bear 5% interest and are in denominations of $100, $500, and $1000, with various maturities. They are placed in the open market and are sold to investors in all parts of the country and have even been sold in foreign countries for they are considered as safe and as well secured as any municipal, or state bond and besides bear a good rate of interest.
IV

THE NEED FOR BETTER RURAL CREDIT FACILITIES IN THE UNITED STATES

It has been said with truth that agriculture is the basic industry of the United States. We, as Americans, have taken great pride in our agriculture and have pointed out that in this field we lead the world. It is true that we have led the world in applying mechanical inventions to the farm and thus making possible large scale farming; and in several other fields we have been notably successful. But on the other hand we have neglected to take some precautions which are essential for the continued success of the American farmer. To-day, certain signs of weakness are becoming apparent to the careful observer.

Among these signs is the growth of farm tenancy, which is becoming a great problem. During the last decade the number of tenants increased about 16%, while the total number of farmers owning and living on their farms increased but 8%. Between 1890 and 1900, the total number of tenants increased 56% and in the previous decade the increase was 30%. To-day, 38% of our farms are operated by tenants rather than by farm owners.

This growth of tenancy has certain features which are not for the best interests of American agriculture. Any tenancy

1 Joint Hearings Before the Sub-Committees of the House and Senate, Investigating the Subject of Rural Credits, p. 158.
system tends to rob the soil of its fertility and especially is this true if the rent be paid by a share of the produce as is the case in two-thirds of the rented farms. The farm is leased for three or five years at the longest and in many cases for only one year, and for this reason the tenant does not have a permanent interest in the upbuilding of the farm. He plants crops which are destructive of the fertility of the soil, and as a rule entirely neglects to put a proper system of crop rotation into operation. Crops such as clover and other legumes which restore fertility to the soil are not raised for they are not as directly profitable as are other crops which exhaust the natural fertility of the soil. Besides this, the tenant does not take an interest in keeping the fences and buildings in repair; and he neglects the many little things that although small in themselves taken together are hard on the farm. The tenant lacks a permanent interest in the community and because of this he is slow in doing his share in its upbuilding. He objects to paying a proper tax for schools and good roads, and the seriousness of the country church problem is possibly but an outgrowth of the rapid growth of tenancy.

Furthermore, the effect on the tenant himself must be considered. It is an old adage that "A rolling stone gathers no moss", and in no case is it more applicable than to the American "renter". Equally true and applicable is the saying that "Three

removes are as good as a fire". The farmer who is constantly changing from one farm to another is the man who comes up to his old age without having accumulated a competence.

A study of modern agricultural conditions will show that the farm of to-day is a business institution of no small size. The Department of Agriculture states that one hundred acres is the smallest sized farm that can be handled efficiently.\textsuperscript{1} Under modern conditions a smaller unit than this must involve waste of labor and equipment. To compete with other producers each farm must have modern labor saving machinery. A farm of the above size can be handled efficiently with one, or in some cases, two, of the new machines. One gang plow, one harrow, two corn cultivators, one grain binder, and other like tools, will do the work, and if the farm be less than one hundred acres in size, the machines will not be worked to capacity and a loss will result. The above machinery requires at least four horses as motive power. Enough work must be required to keep these horses busy most of the time, or further loss will result. Another reason for fixing one hundred acres as the minimum size is that a proper rotation of crops will require at least this much land. Farm buildings are expensive and one set of buildings will do as well for a farm of this size as for a smaller one, and thus an economy can be brought about. As a matter of

\textsuperscript{1} Joint Hearings Before the Sub-Committees of the House and Senate, Investigating the Subject of Rural Credits, p. 74.
fact the average farm contains 138 acres\(^1\) and very few farms in the great agricultural states are smaller than 160 acres.

It is evident that the initial outlay for the farm must be large and to this cost must be added the constantly increasing amount that must be spent for equipment of all kinds. One expensive item in many states is the purchase of commercial fertilizers, the expenditure for which increased 115% between 1900 and 1910.\(^2\) All these items combined require an outlay that is almost beyond the power of the young farmer to make. The average wage for farm hands, even in the best agricultural states, is not over $30 per month. It would require a lifetime for a young farm hand to acquire enough to make even the first payment on a farm. As a matter of fact, most men who own farms in our best farming states have either inherited them or have purchased them when the country was newly settled and the price of the land was only a small fraction of its present value. The young men who have wished to acquire farms have gone westward and northward in ever-increasing numbers, but today the supply of cheap land in the United States is nearly exhausted and the problem of acquiring a farm is becoming more difficult. These facts go to explain the growth of tenancy already considered and show that a supply of ready credit is a necessity for the efficient conduct of the modern farm.

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The need of better credit facilities is equally well shown by a study of mortgages on the 62% of the farms which are worked by their owners. The census of 1910 shows that 34% of these farms were mortgaged, this being a larger percentage of mortgaged farms than had been shown by any previous census. The average mortgage in 1910 was for $1715 as compared with $1234 in 1900, but this increase is in part at least due to the increase in the value of the farms, which was more than one hundred per cent during the same period. The largest proportion of the mortgages are put on the farm to pay the purchase price, so that the increase in the value of the land would easily explain this increase in the size of the mortgage.

Dr. J. L. Coulter, who was formerly connected with the Department of Agriculture, made a study of farm mortgages which enabled him to discover some interesting facts. He found that the mortgaged farms are ten acres larger and have eighteen acres more of cultivated land on the average, than do the unmortgaged farms. The average value of mortgaged farms was $4,910, while the value of unmortgaged farms was but $3,558. The value of buildings on mortgaged farms was $200 greater than on the unmortgaged farms, and the value of the equipment was $75 more on the mortgaged farms. He concluded that the money borrowed on mortgages is being used to buy more land and equipment and

2. Mormon's Principles of Rural Credits, p. 190.
3. Hearings before the Joint Committee of the House and Senate, pp. 154-155.
to build better buildings. In other words, the modern farmer is not afraid to go in debt if he finds that his profits will thereby be increased.

The above facts in regard to farm loans do not show that the country is in a serious condition. In fact they do not show that anything is fundamentally wrong, for the money borrowed is being used for productive purposes, and debt for that purpose is only a means of additional profit. In fact our best agricultural states, such as Iowa, Illinois, Wisconsin, Kansas, Indiana and Ohio, have a larger proportion of mortgaged farms than do the poorer states. Fifty-one per cent of Iowa farms are mortgaged.\(^1\) The problem is not to do away with mortgage indebtedness or even to reduce it, but rather to establish a system whereby the farmer may be on a par with the business man of equal security and thus obtain the favorable rates and conditions of repayment to which he is entitled.

There are five common sources or places where the farmer has been able to obtain long time mortgage credit. These were the banks, both state and national; real estate and mortgage brokers; private lenders; life insurance companies; and trust funds held by the state such as the school funds. When a farmer wished to secure a loan he naturally went to his banker. If the loan was to be on real estate security, up to the passage of the Federal Reserve Act, he would have been refused, for

\(^1\) 13th Census of the United States, Abstract, p. 536.
previous to that time, the national banks were not allowed to lend on real estate security. The Reserve Act made about first $200,000,000 available for five-year/mortgage loans\(^1\) by allowing national banks to lend on farm property up to 50% of its value, the total amount which each bank is allowed to lend on this class of security being limited to 25% of its capital and surplus or two-thirds of its time deposits.\(^2\) As the total mortgage indebtedness on the farms of the country is approximately $2,000,000,000,\(^3\) it will be seen that only one tenth of the demand for mortgage loans can be satisfied, even if the banks lend this entire amount on mortgages. In all probability they will not do this for they have not been accustomed to lend on real estate in the past, and they will naturally hesitate to tie up so large a part of their deposits in non-fluid security. Furthermore, the banks have not had more than enough money in the past than was necessary to meet the demand for purely commercial loans and it is unlikely that, even though the supply be increased by the operation of the federal reserve act, they will have surplus funds which they will be willing to invest in long time loans.

Practically all the state banks have been allowed to lend on real estate security, but as a matter of fact very little has been so lent. This is partly due to the fact that they hesitate to tie up their funds in the manner that would be re-

\(^1\) Congressional Record, 63rd Congress, First Session, p. 3203.
\(^2\) Federal Reserve Act, Section 24.
\(^3\) Abstract, p. 235.
quired by such a practice, and partly to the fact that they must deal with national banks and must hold the class of paper that will be accepted by the national banks.

It is true that the banks have apparently been lending a great deal on real estate security, but these loans have been made either by the trust company connected with the bank, or for some one for whom they are acting as an agent. This person may be a private party, either in that neighborhood, or in some distant state, for whom they are acting as local agent because of their knowledge of local conditions. Many banks act as agents for life insurance companies, lending the funds which these companies accumulate through premium payments, and which they are holding as a reserve. Most of the states require that these reserve funds be invested in real estate mortgages, and many of the companies have chosen to place them on farms. However, they are in general confined to loans to the farmers of the middle western states, as a matter of fact lending only in a comparatively few states. Iowa farmers have 31% of the farm loans made by the insurance companies and only pay an average of 5.6% on the money.\(^1\) The insurance companies limit their loans to the best farming sections because they furnish the best security. As will be shown below, the mortgage situation in these states does not present the problem that it does in other sections of the country, because the high class of security

\(^1\) Mormon's Principles of Rural Credits, p. 213.
offered enables the farmers to obtain their loans at a low rate of interest. For these reasons it is evident that loans made by life insurance companies will not solve the problem.

A third and perhaps the most important source of mortgage loans is the real estate and mortgage broker. In some cases he acts as the agent of a life insurance company or other foreign investor, but in most cases he represents a local investor who is seeking a safe investment for his funds at as high a rate of interest as is possible. Especially in the western states he is the agent of eastern capitalists who employ him to place their loans because of his knowledge of local conditions. He not only places the loans, but he collects the interest and represents the investor in all matters. Whatever may be the source of the loans made by the broker, it is evident that he must receive some remuneration for his services, and it is also evident that this must be added to the cost of the loan. Two methods are adopted. He may receive his commission directly from the person making the loan. If so, the debtor must pay this commission directly in the form of a higher interest rate. The more common method, however, is for the broker to deduct this commission directly from the face of the loan. Thus, on a $1,000 loan the borrower may receive but $950, the balance going to pay the commission of the broker. It is evident that the wastefulness of this method could be avoided by some method of standardizing
the loan, similar to the European methods.

A somewhat less important source of loans is the local capitalist who makes the loan directly without the aid of the broker or banker. These capitalists are largely confined to the eastern or central states, since the western and southern states have not as yet accumulated surplus funds to be so invested. The number of loans which they can make is also very limited for the modern farm mortgage is so large that it is beyond the reach of the local capitalist. Still another source of funds is the school and other trust funds held by some of the states, especially in the central west. These funds are lent through one of the county officers and are placed only after the property to be mortgaged has been appraised by a committee appointed for that purpose. The total amount of these loans is so small that they do not form an important factor.

The foregoing discussion has considered conditions in general, but a somewhat more detailed study will show more of the actual facts as we find them in different parts of the country. The group of states commonly known as the New England states presents a situation that is quite different from the rest of the country. These states have been settled and have been farmed for so many years that the demand for capital with which to acquire farms is not as keen as in some of the newer states. The farms in general pass from father to son and hence capital is not needed to meet the first cost. This section, having
been settled for many years, is blessed with a large amount of capital seeking investment. For this reason there is no difficulty in securing first mortgage loans at 5½% or 6%.
The committees from these states unite in saying that the need is not for more or cheaper money, but for some system which will provide for the amortization of the principal of the loan. The local capitalists are not willing to lend except for definite periods and will not give the borrower a chance to reduce the principal during the life of the loan.

However adequate may be the supply of money for long time loans, there is a demand for short time loans. The run down farms of this section demand large quantities of commercial fertilizer, and the proprietor must borrow money for this purpose for from six to nine months. This is but one of the sources of the demand for short time loans. At present the only way by which such loans can be secured is by giving chattel mortgages, but this class of security is very unpopular both with the lender and the borrower. In many cases the merchant "carries" the farmer on his books until the crop can be sold, but this is a very expensive method of obtaining credit. The cooperative savings banks in the New England states also meet a part of the demand, but in general the farmer pays more than does the business man who is able to give the same class of security.
Massachusetts and New York have attempted to meet this need by the organization of credit unions as described above, but in both of these states the unions that have been formed have been confined to urban rather than rural communities. The failure of these unions to meet the needs of the rural sections will be discussed below. New York by the organization of the Land Bank of the State of New York has attempted to meet the need for long time loans at favorable rates of interest and favorable conditions of repayment. It is hoped that this bank will meet the need for long time loans in New York.

A consideration of the entire group of states known as "The South" shows much the same condition in all of them and it is in these states that the need for both better and cheaper credit for both long and short periods is most keenly felt. Following the Civil War an entire change in the social and economic organization of this section took place. Previous to this time the plantation system of agriculture had almost exclusively prevailed. The farms were large and were worked by slave labor, the management being largely centralized. When the slaves were freed, it was necessary to divide these farms into small tracts and either sell or rent them to the freedmen. The slaves, of course, had no capital and hence it was necessary

1 See Chapter III, Section
2 See Chapter IV.
3 See Chapter III, Section
to adopt the "crop lien" system of financing the farms. The owner of the land would rent a small tract to one of the former slaves and besides furnishing the land and buildings would also furnish the seed, equipment and even the food and clothing of the tenant and his family. When the crop was gathered, the owner of the land would be paid for all advances as well as for the rent of the land, the payment generally being a share of the produce. If the crop was good, the tenant would have enough left after the landlord had been paid, to support himself until the next crop could be raised, but in general he would again be destitute at the beginning of the season and the process would be repeated. In only a very few cases did the tenant raise enough so that he would have a surplus at the end of the year, and that was generally squandered for the newly made freedmen did not know how to use their new freedom.

The owner of the plantation was generally compelled to borrow in order to supply the tenant with seed and equipment, for in most cases he owned nothing but the land. A wholesale supply merchant was generally given a mortgage on the prospective crops of all the tenants and he would then furnish the needed supplies to the landlord. Thus the system tended to keep both landlord and tenant under the control of the city merchant or capitalist, and most of the weaknesses of present day agriculture are but the outgrowth of the crop lien system and the conditions which it developed.
The crop lien system as used in the south to-day is but a modification of the system just described. Instead of the tenant going to his landlord for seed and equipment, he more frequently goes to the crossroads merchant and there secures the advances required, giving a mortgage on the crop to be raised and in many cases, on live stock and furniture as well. The opportunity to make this class of loans soon attracted the money lenders from the city to the country districts where they opened stores not so much for the purpose of retailing goods for a profit as for the purpose of making loans at an exorbitant rate of interest. To-day the tenant is forced to go to these merchants and ask for credit, which is granted after the borrower agrees to raise a certain number of acres of corn or cotton. A mortgage is given on the crop, and thus the tenant farmer is financed until the crop can be sold. The raising of the crop is then under the direction of the merchant who makes the loan. He hires agents to inspect the growing crop at regular intervals, and if it is thought at any time that the prospect for a good crop is poor, and that the loan is insufficiently secured, the borrower is required to give additional security, or have his credit reduced. This system places the farmer entirely under the control of the merchant for book credit rather than cash is given in every case. The merchant generally charges from 25 to 50 per cent more for goods sold in this way than for those
sold for cash, and so makes a large profit on the goods, besides the high rate of interest that he secures on the loan. This rate is never less than 10 per cent and in many cases it is as high as 12 or 15 per cent.

Another evil is that only cotton, tobacco, or other cash crops can be raised, for the merchant must be able to sell the crop as soon as it is harvested. This confines the south to the raising of a comparatively small number of crops and the gains to be obtained from diversified farming are lost to the nation. The merchant generally reserves the right to buy the crop when matured, and so he is enabled to pay as low a price as he desires, for the laws against selling a mortgaged crop, would prevent the tenant from selling the crop to anyone else. In perhaps the majority of cases in the south, to-day, as far as can be learned from a study of conditions there, the tenant has just about enough from his crop at the end of the year to pay the merchant for the loan, and in very few cases does he have a surplus left for a reward for his undertaking. Thus the largest part of the tenants, both black and white, have been and still are under the control of the money lenders and this explains in a large part the backwardness of the south from an agricultural standpoint.

That the crop lien system as just described still continues is although slightly modified by the laws of some of the
states is shown by a personal letter from Mr. J. H. Reynolds, President of the First National Bank of Rome, Georgia. He states that the crop lien system is still used to a great extent, the "cropper" paying from 25 to 50 per cent profit on all goods bought from the merchants on time. Professor J. W. Bell of the University of Mississippi writes that the system is still used and probably will be for a good many years to come. He says that the south fully appreciates the evils of the system, but as the ownership of the land by the farmer is not increasing rapidly if at all, he sees no relief unless it be in some form of cooperative credit, and he greatly doubts the practicability of any such system in the south.

The committees appointed at the request of the American Commission to investigate the rural credit situation in South Carolina states that there is great need for short time credit facilities to enable the farmers to escape from the present ruinous crop lien system. They add that if the farmer could command cash at a reasonable rate of interest for buying seed, fertilizer, and implements and for hiring labor, it would work wonders in the upbuilding of the south. At present $300,000,000 of agricultural wealth is produced annually in the state and nine-tenths of it immediately vanishes to purchase goods which could be produced at home if proper credit facilities were obtainable. ¹ The North Carolina Committee concludes that the

farmers pay from 20 to 30 per cent on loans in normal years.\(^1\) The Tennessee committee states that an efficient rural credit system would make that state a leader in agriculture.\(^2\)

An investigation under the direction of Dr. Lewis H. Haney of the University of Texas showed that the average rate on long time mortgage loans in Texas is about 10 per cent at the present time.\(^3\) Dr. Haney testified before the Federal Industrial Relations Committee on March 19, 1915, that over one-third of the farmers of Texas pay more than the legal rate of interest.\(^4\) The committees which investigated the credit situation in nearly all of the southern states unite in the conclusion that the crop lien and other credit systems as used in the south to-day are costing the farmers too much for interest and are holding back the industrial development of the south. These committees also state that long time credit facilities consist mostly of loans from northern capitalists at about 8 per cent besides an average of 2 per cent for commissions paid to the agent from whom the loan is obtained.

The committee appointed by the Governor of North Carolina to investigate rural credit conditions in that state says:

"There is a great need for a large state land mortgage bank,


\(^3\) Haney's *Studies in Agricultural Economics*, p. 6.

\(^4\) *Chicago Tribune*, March 20, 1915."
or some similar system which would mass the mortgages and issue bonds against them, thus making available a supply of 5 per cent money which is already within the state but which will not be invested in farm mortgages under the present system.

These statements show that there is the same need in the southern states that we find in all parts of the country. Some system of massing mortgages and issuing bonds against them, combined with provisions for the amortization of the principal, is essential and must be established either under state or federal control.

The three new states, Oklahoma, New Mexico and Arizona, show conditions which are somewhat different but which point to the same need. These states have been settled in comparatively recent times and their agricultural possibilities, and hence the security back of the loan, are unknown. Eastern capitalists are slow to invest in these states and hence first class properties must pay an exorbitant rate of interest. The rate on short time loans in New Mexico averages over 12 per cent.

Real estate loans are generally made for three years or less and bear at least 10 per cent interest. A few insurance companies are beginning to lend in these states but they charge 7 per cent on the loan and require the borrower to take out a policy with the company, which brings the cost of the loan up

1 Agricultural Cooperation and Rural Credit in Europe, Part 3, American Evidence, p. 50.

2 Agricultural Cooperation and Rural Credit in Europe, Part 3, American Evidence, p. 46.
to 12 or 15 per cent. The policy is assigned the company as additional collateral. In addition to the above cost, these 7 per cent loans are frequently discounted at 3½ per annum on the face of the loan. Thus on a 7 per cent loan the actual interest would be over 11 per cent, besides the premium on the insurance policy. The land in these states is first class security for its earning power per acre is as great or greater than the best farm lands of the eastern and central states. This statement is substantiated by the fact that the farmers in these states have prospered although paying from 10 to 15 per cent interest on their investment, a rate which the farmers of the other states could not afford to pay. A system which will furnish these farmers with the money which they need for the development of their lands, at a rate which the security that they can offer entitles them to, is a definite requirement of the immediate future.

The states north of the Ohio and Missouri rivers and between the Appalachian and Rocky mountains contain the most highly developed and perhaps the best farming areas of the entire United States. Here modern scientific farming has reached its greatest development and the future possibilities of the states are just coming to be realized. It can be said that this section does not need an improved credit system as badly as do the southern states, but even in this highly pros-
perous section, the farmers are at a great disadvantage in bor-
rowing as compared with the merchants of the same states. Here
we find much the same condition as in the sections already con-
sidered. The banker prefers to lend to the merchant rather
than to the farmer. One reason for this preference is that
the farmer is not business-like in his dealings with the banker.
He is not prompt in meeting obligations when due. He prefers
to pay by cash rather than by check, thus requiring cash rather
than book credit when a loan is made to him. His security is
generally located at some distance from the bank and hence
expense and delay are involved in its inspection, and especially
is this true of the smaller loans secured by chattel mortgages.
On the other hand, the banker knows the merchant personally
and associates with him in his daily life. He meets him in
the clubs and entertains him as a guest in his home. Hence
he knows something of his personal characteristics and reputa-
tion, factors which must be considered in making a loan. The
banker knows little or nothing of the personal habits and
characteristics of his farmer client and has no opportunity
of meeting him and knowing him personally. The banker is
able to inspect the security offered by the merchant or pro-
fessional man with little or no expense or loss of time. For
these reasons it is not strange that the average banker is more
willing to lend to the business man than to the farmer. These
conditions have all combined to make it difficult for the farmer to secure a sufficient amount of capital to properly conduct his business, and have required him to pay an exorbitant rate of interest on the sums that he has been able to secure.

The usual plan for securing a long time loan for the purpose of buying a farm in this section is as follows. The funds are obtained from one of the five sources mentioned above, the preliminary steps varying according to the source of the loan. The time of the loan is generally five years, but in some cases loans are made for three years and occasionally one is made for ten years. The borrower gives a first mortgage on the property, furnishes a satisfactory abstract of title and gives an insurance policy on the buildings to the holder of the mortgage. Payments on the principal are occasionally allowed on interest paying dates, but the more common practice is to allow the principal to be paid only at maturity. This is because the private investor is not able to use to advantage, the small sums by which the principal would be reduced, if payments were allowed annually. He must keep his funds invested in one place and hence requires the borrower to retain the entire amount borrowed until the loan matures. The rate differs in various parts of the central west. In the states east of the Mississippi, owing to the fact that they have settled for a comparatively long time, capital is somewhat abundant and can be secured for long time loans at
5 or 6 per cent.\(^1\) A possible exception to this statement are the "cutover" sections of Wisconsin and Michigan, where agriculture is just beginning to be placed on a firm basis and hence the farmer is required to pay as high as 8 per cent on mortgage loans.

It is probably true that Iowa has both the most available capital and the lowest interest rate of any state in the union. This is due to the fact that it is in many respects the leading farming state. Investors know that Iowa lands furnish very high class security and are willing to invest their funds in this kind of security, even though competition forces them to take a lower interest rate than could be secured in other states. As mentioned above, 31 per cent of the reserve funds of life insurance companies that are invested in real estate mortgages are on Iowa land. The average rate of first mortgage loans is perhaps 5\(\frac{1}{2}\) per cent in eastern and southern Iowa and 6 per cent in the northern and western counties.\(^2\) The rate on short time loans unsecured, or secured by collateral mortgages averages about 7 3/4 per cent.\(^3\) Nebraska shows a great variation in the different parts of the state. The eastern counties pay about 6 percent on mortgages but the rate runs up to 12 per cent in the western part of the state.\(^4\)

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1 The Road to Cheaper Money, p. 3.
2 The Road to Cheaper Money, p. 18.
4 The Road to Cheaper Money, p. 20.
The committee appointed to investigate credit conditions in Minnesota reports that long time loans vary from $5\frac{1}{2}$ per cent to 10 per cent in the different parts of the state, the latter rate being on mortgages in the northern sections. Loans on wheat land in the Red River valley can be obtained for 8 per cent. The committee also reports that the rate varies greatly between sections only a few miles apart, depending on purely local conditions. The rate on short time loans varies from 6 per cent to 12 per cent depending on the section and the security offered.

As would be expected, the Dakota farmer pays a higher rate of interest than does the farmer of the older states. An investigation made by the Farm, Stock and Home, a paper of Minneapolis, Minnesota, showed that the rate in these two states runs from 6 per cent in a few of the best counties of South Dakota, to 10 per cent in the western part of the same state. The Montana farmer pays 10 per cent or more. The usual length of loans in these states is three years or less, thus making the cost of renewals a large part of the total cost of the loan. The money must be brought from the eastern states and a commission must be paid for the services of the banker or broker whenever the loan is renewed. Short time loans in the Dakotas vary from 8 per cent to 12 per cent, very few being made for less than 10 per cent.

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1 Agricultural Coöperaion and Rural Credit in Europe, Part 3, American Evidence, p. 34.
2 The Road to Cheaper Money, p. 3.
3 The Road to Cheaper Money, p. 3.
To the interest rates mentioned above, must be added certain charges, chief among which is the commission charged by the broker. The cost of the abstract of title is considerable, but perhaps is not as great as in the older states, where the title is more involved because of the many transfers that have been made. It is also customary in the newer states to deduct the first year's interest when the loan is made. This raises the rate paid on the actual money received about 1 percent in most cases.

Agriculture in the Rocky Mountain and Pacific coast states is so comparatively unimportant that the needs of the farmer in these states have attracted but little attention. It is sufficient to say that the farmer and fruit raiser of these states has many of the same difficulties that his brethren of the eastern states are forced to face. The Washington committee reports that a system of long time loans repayable by amortization is needed and that in their opinion a system modelled after the Land-schaften unions would be practicable. There is also a need for short time loans at a lower rate of interest.\(^1\) The committee which studied credit conditions in Oregon states that rural interest rates are too high in that state, and that the terms of payment are not suited to the farmer.\(^2\) These two statements may be taken as showing that conditions in these

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1 Agricultural Cooperation and Rural Credit in Europe, Part 3, American Evidence, p. 59.
states are the same as in other sections, the demand being for cheaper money and some plan which will include the amortization principle.

It will be seen from the foregoing discussion that the need is not for cheaper money alone, but for longer loans and the privilege of paying off a part of the principal each year. The price of land has reached such a figure that it is no longer possible for a young man to buy a farm and pay for it during the life of a three, five or even seven year loan. The best that he can hope to do, if he depends entirely on the produce of the farm, is to keep up the interest, and perhaps accumulate the purchase price in 25 or 30 years. In most cases he is able to accumulate a little surplus over the interest charge each year and he should have the benefit of some plan whereby he could apply this surplus to the reduction of the principal. Under our present system of private loans he must put the money in the savings bank at a low rate of interest and hold it there until the mortgage note becomes due. This involves a loss, for in practically every case he is paying a higher rate on the mortgage than he is getting for his savings in the bank. There is also a temptation to spend the accumulated funds in some way rather than to hold them for the repayment of the principal when due. The loss of interest and the danger of spending accumulated funds could be avoided if the principal could be reduced at any interest paying date. The farmers of this country should have
a system whereby it would be possible for them to secure a loan for 35 or 30 years and by paying 6 or 7 per cent a year during the life of the loan, not only pay the interest but pay the principal as well. That this would be both possible and practicable was shown above, under the discussion of the Land Bank of the State of New York\(^1\) as well as by the description of the Landschaften and other European systems of mortgage loans. A discussion of a possible plan for meeting this need will be the theme of the next division of this paper.

\(^1\) See Chapter II, Section 9.
A PLAN FOR IMPROVED RURAL CREDIT FACILITIES IN THE UNITED STATES

The demand for improved rural credit facilities in the United States takes two forms. Cheaper money for short time loans, and some system of long time loans which will both reduce the interest rate now paid on such loans and provide a method whereby the principal may be repaid, at least in part, before the maturity of the loan, are demanded. The conditions which make imperative some provision for meeting these needs have been discussed in the preceding chapter of this paper.

The various plans which have been suggested for furnishing short time loans to the farmers have been modelled to a large extent upon the Raiffeisen and similar systems abroad. Wisconsin and Texas have provided for cooperative credit unions of this type, but as shown above, no unions have as yet been organized in these states. New York and Massachusetts also have laws authorizing unions of this type, and in these states some unions have been formed, but without exception they have been organized in the industrial centers rather than in the rural communities. The cooperative credit union has not proved to be a success in the United States. Some of the reasons for the lack of success follow.

1 See Chapter 3, Section 6.
There are two types of credit unions. In one type the members assume unlimited responsibility for each others' debts, and in the other type the responsibility is limited to the value of the stock held in the union, or to twice the value of the stock. In either case the security given is largely personal. That is, these unions are organized for the purpose of obtaining and granting credit on the combined resources of the members. Honesty, industry and sobriety are believed to be sufficient guarantees for the repayment of a loan, and hence if a member is granted a loan these personal characteristics are the security given, rather than a mortgage or some form of collateral. Thus under either plan of liability, the association or union assumes the risk of being compelled to pay a loss caused by the failure of a borrower to repay a loan. The risk assumed is the same in either case and the possible loss differs only in degree, in either a limited or unlimited liability system.

For the successful operation of such a system, certain requirements must be met which, so far, our American rural communities have failed to meet. The members composing such an association must know each other thoroughly. They must belong to a small community where each member knows every other member of the union personally. This acquaintance must extend not only to a general knowledge of the people, but must include also a knowledge of their family life, and connections, their honesty
and thrift, and their business relations. In short, it must include an intimate knowledge of each aspect of the life of their neighbors. They must be in a position to watch the purpose to which a loan is put, for it must be used for the purpose for which it was borrowed, or it will, in most cases, not be safe. They must watch the crops of all their fellow members and see that they are properly taken care of, or the borrower will not be able to repay his loan when it is due. In fact, each member of a cooperative credit union must be a spy on every act of his fellow members.

This sort of organization is not adapted to American conditions. The residents of our rural communities are constantly changing, and especially is the tendency marked where the tenant is predominant. This constant change makes it impossible for the American farmer to know his neighbor well, for he cannot know him long enough to gain more than a general impression of his character. If he is to assume responsibility for his neighbor's debts, he must supervise his neighbor's actions, and this kind of supervision does not conform to our American standards of liberty. The American farmer will not watch the actions of his neighbors closely nor will he allow his neighbor to dictate to him as to his conduct. These facts combined with the constantly changing and shifting population of our rural communities, have prevented the organization of cooperative credit unions among our farmers. These unions could do a great deal
of good, could they be successfully conducted; but until
our country becomes older, progress towards their formation
must continue to be slow, however favorable state and federal
laws may be.

The fact that the unions have been successful among cer-
tain Jewish farmers and in the industrial centers of Massa-
chusetts, but bears out the conclusion that they will continue
to fail of success among typical American farmers. Among the
mill hands and the Jewish farmers there is sufficient community
of interest, and a sufficiently stable population to make the
operation of the unions possible.

Many plans for a system of granting long time loans have
been proposed. These plans have this in common, viz., that
the funds from which the loans are to be made, are to be se-
cured by the sale of bonds secured by the first mortgages given
on the property upon which the loans are made. The attempt of
New York to solve the problem by the formation of the Land
Bank of the State of New York has been discussed above.¹ This
plan seems to show great promise, for it is adopted to the
conditions in New York. However, it is doubtful if the plan
could be generally adopted throughout the country for the
building and loan associations upon which it is based, are
not found in many of the states.

¹ See Chapter 1, Section 5.
Many of the plans suggested have provided for the organization of banks under state authority for the purpose of selling bonds and loaning the money thus obtained on real estate mortgages. A bill providing for such a bank was introduced in the Iowa legislature during the session of 1915, but after passing the House it was defeated in the Senate. Similar bills have been defeated in other states. A possible explanation of the failure of these bills to become laws, is the growing conviction that a system of the size commensurate with the demand for mortgage loans should be organized under federal rather than under state control. The difficulty of putting in operation a system based on land mortgages, when the different states have varying laws relating to mortgages, foreclosures, deeds, titles, and the taxation of mortgages, is recognized. It is thought, however, that this lack of uniformity can be corrected by giving the board in control of the national system, the power to withhold the right of organizing the banks for which it provides, until the laws of the state have been changed to meet the approval of this board, or to conform to certain definite requirements which it will lay down.

It is unnecessary to describe or discuss in detail all the plans which have been proposed for land banks and credit unions, for the best features of each bill have been included in the Hollis-Bulkeley bill, the history of which was given in the introduction to this paper. This bill represents the most
careful thought and consideration that has yet been given to any bill or proposed plan, and altogether seems to provide for the most practicable system yet devised. It follows the lines of the Federal Reserve System of banking in general and the type of banks for which it provides would supplement that system. For this reason it is thought that the plan which is finally adopted will be based on the plan proposed by this bill.

The control and direction of the credit system proposed by the Hollis-Bulkeley bill is placed in the hands of a Federal Farm Loan Board, consisting of three members, two of whom the Secretary of the Treasury and the Secretary of Agriculture are members ex officio. The third member is a new official called the Commissioner of Farm Loans. He is to be appointed by the President of the United States and is to have general executive control of the entire organization. The law provides that national farm loan associations can be organized by any number of persons, not less than five. These associations are to be the units for making loans to the farmers who unite to form the associations. The officers are to be, a president, a vice-president, a secretary and a treasurer. These officials are to be chosen from the membership of the board of directors, who are to be elected by the stockholders. The stock of each association is to be at least $10,000, divided
into shares of $25 each. Each stockholder is entitled to one vote for each share of stock held up to two votes. Two plans are provided for the issue of shares. They may be entirely paid up when issued or only 10 per cent of their value may be paid in at first, the remainder being paid in equal annual or semi-annual payments. This latter plan is the one which is used by the building and loan associations of the country. In fact, these proposed loan associations resemble the building and loan associations in many ways. The objects to be attained by the two associations are similar; the main difference being that the loan associations will lend on farm property rather than on city property, and that monthly payments will not be required on the amount borrowed as in the building and loan associations.

One thing which must be carefully guarded against, is the danger of appraising the property to be mortgaged at too high a figure in order to obtain a large loan. Nearly as many different methods as plans, have been proposed for guarding against this danger but none of them seem to be entirely satisfactory. The Hollis-Bulkeley bill provides for the appointment by the board of directors of two of its members to act as members of the appraisal board of the association. The third member of the board is to be some resident of the community to be selected by the board of directors of the dis-
strict bank. He is to be a man who is fully conversant with land values, but cannot hold stock in the association. All farms to be mortgaged must be valued by this board and the amount of the loan granted cannot exceed 50 per cent of the value so determined. This form of committee is perhaps as good as any, but the chief danger lies in the tendency of the board to be influenced by personal considerations or perhaps by an exalted idea of land values in that particular community and to a large extent upon the honesty and careful judgment of the members of this appraisal committee.

As soon as one half of the capital stock has been paid in, the association can proceed to make loans to its members, using the capital as a loan fund. Before a loan can be made, the member must hold shares of stock equal to five per cent of the amount of the loan desired. Each mortgage is to run for not less than five years and not more than twenty-five years. It must provide for the repayment of the loan either in whole or in part, at any interest paying date after five years from the date of the loan. It must also contain a requirement for the reduction of the principal of the loan by annual or semi-annual payments in addition to the interest payments. This requirement is perhaps the most important part of the plan for it meets the greatest need of the American farmer, viz., opportunity to repay the principal of a loan in small annual payments instead of the necessity of holding accumulated funds until the
loan matures. This provision combined with the lowering of the interest rate which will be made possible because of the increased capital which will be available through the sale of bonds, will make it possible for the young farmer to acquire and pay for a farm in the best farming sections of the country.

Loans obtained as described above must be used for one of the following purposes: to improve farm lands; to purchase a farm; to purchase live stock and equipment for use on a farm, or to liquidate indebtedness existing at the time when the loan is obtained or subsequently incurred for any of the above purposes. Thus the loan is limited to productive purposes only and hence cannot be used for speculation. This restriction is important; for otherwise debts might be incurred which could not be repaid from the increased production resulting from the use of money borrowed. The success of the system would depend, in a large measure, upon the precautions taken by the local associations to make this restriction effective. Another wise regulation is found in the provision that a loan can be made only to a person who is or is about to become a resident on the property mortgaged. This will insure the operation of the system for the benefit of resident home owners and not for the good of absentee landlords.

It is provided that if the demand for loans is not large enough to require the investment of the entire capital of the
association in farm loans, the surplus may be invested in the bonds of any other association or in government bonds. If, as will no doubt be the case, the demand for loans is greater than can be supplied from the capital of the association, additional funds can be obtained by pledging the mortgages already held with the Federal Land Bank of that district.

This district bank is to be one of twelve in the entire country. The United States is to be divided into twelve districts corresponding as nearly as possible to the twelve districts by the Federal Reserve banking system. No state can be divided into fractional parts for these land bank districts and hence they cannot correspond exactly to the Reserve districts. The Federal Land Bank may have its office in any city of the district in which it operates.

This district Federal Land Bank is to be formed by five of the local associations which unite and organize it. It is to be governed by a board of nine directors, three of whom will be appointed by the Federal Farm Loan Board, and six of whom shall be elected by the local associations uniting to organize the district bank. Its capital which shall be at least $50,000 before it can issue bonds, may be obtained in three different ways. Before the local associations can transfer mortgages to this district bank they must have at least ten per cent of their capital invested in the capital
stock of the district bank. This will provide the largest portion of the capital, if not all of it. Private parties may hold its stock if they so desire, and in order to make the subscription of the minimum capital, $50,000 certain, the act provides that if after the subscription books have been open ninety days, the total has not yet been subscribed, the Secretary of the Treasury shall purchase the remaining stock for the federal government.

The main purpose of the district land banks is the issue of bonds secured by the mortgages pledged to it by the local associations which have taken the mortgages as security for loans upon farm land. The capital of the local associations is far too small to meet the demand for loans that will surely come to them, and so additional funds are to be provided by the issue of bonds by the district bank. When the district bank receives a mortgage or mortgages from a local association, it will deposit them with the Federal Reserve Agent of the Federal Reserve Act district. He will examine these mortgages and if they are found to be satisfactory, he will authorize the issue of bonds secured by these mortgages. Proper precautions to prevent the over issue of bonds are provided and as this officer is an agent of the federal government, through the Federal Reserve Board, he is a disinterested party and will see that the provisions of the act are carefully carried out.
The local association will collect the payments for both interest and the amortization of the principal, and will turn over to the district bank all payments made on mortgages held by it. It is provided that additional mortgages must be deposited with the Reserve Agent to cover the decreased value of the mortgages held by him, caused by the reduction of the amount of the principal remaining unpaid. All payments on the principal of a mortgage held by the Federal Reserve Agent are to be credited on the mortgage and when the principal is paid in full, the mortgage will be returned to the local association and through it to the maker of the mortgage. This phase of the operation of the act, corresponds almost exactly to the discounting of commercial paper by the member banks with the new Federal Reserve Banks, and has a similar purpose, the only difference being that the loans are for long rather than for short periods of time.

The Federal Farm Loan Board, which has the general control of the system, is given the power of fixing the interest rate for each district and also the rate of interest which the bonds of the district bank shall bear. It is intended that these rates shall be as nearly alike as possible for all of the districts, but this may not be possible and so the federal board is to determine the rate for each district. In general the rate of interest will be one per cent higher than the rate paid on the bonds.
This one per cent will be used to meet the expense of operating both the district banks and the local associations and will be divided equally between them. Any surplus which is left will be divided among the stockholders in the form of dividends. During the first years of the association's existence, one-fourth of the net profits must be set aside as a reserve fund to meet all extraordinary demands. When these reserve funds reach 20 per cent of the capital stock, the entire profits will be divided among the stockholders.

In order to keep the interest rate on mortgages as low as possible, the bonds are to be exempt from all federal, state and local taxation. The capital stock, reserve and surplus of all the associations are also to be exempt from taxation. In order to aid in providing a ready market for the bonds of the district banks, the trustees of the deposits in the postal savings bank are given the right to invest such deposits in the purchase of these bonds. This description has shown that in general the recommended system follows the lines of the Federal Reserve System of Commercial Banking. It is intended to supplement that system and to do for the farmers of the country, what that system does for the commercial interests of the cities and towns. It provides a safe and a sane method of issuing bonds secured by first mortgages on farm lands and for the loaning of such funds to the farmers of the country. In
addition to this it will tend to lower the rates which must be charged the farmers for their loans and will give the borrower the opportunity of reducing the principal of his note by annual payments. Thus it meets the needs which have been shown to exist and at the same time seems to be a safe and practicable system in every respect. For this reason, it is believed that it is the best system which has as yet been proposed, and that it is likely to be used as the basis of future legislation on the subject.
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