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## The Origin and Mechanism of the Clearing House.

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ADDRESSING the Canadian Club upon this subject Mr. J. P. Knight, of Montreal, secretary of the Canadian Bankers' Association, said:

*Mr. Chairman and Gentlemen*.—An eminent American Banker, Mr. Jas. G. Cannon, has produced what is possibly the only comprehensive history of clearing-houses. He opens his admirable and interesting work with the question—"What is a clearing-house"? The definition he gives is that of the Supreme Court of the State of Pennsylvania:—"It is an ingenious device to simplify and facilitate the work of the banks in reaching an adjustment and payment of the daily balances due to and from each other at one time and in one place on each day. In practical operation it is a place where all the representatives of the banks in a given city meet, and, under the supervision of a competent committee or officer selected by the associated banks, settle their accounts with each other and make or receive payment of balances, and so clear the transactions of the day for which the settlement is made."

This plain and simple explanation clearly and fully defines the object for which the representatives of Montreal banks meet daily, and, throughout the entire Dominion of Canada, the clearing-house is simply a time and labour-saving device. It has yet to become what Mr. Cannon claims it now is in some cities of the United States—"a medium for united action upon all questions affecting the mutual welfare and prosperity of its members." Several efforts have been made by the bank managers of Montreal to widen the scope and extend the functions of the clearing-house of the Canadian Metropolis: but the efforts in the direction of fixing uniform rates of exchange and interest, collection charges, and the cancelling of reciprocal arrangements for doing business for nothing, are yet in the rocking chair stage of "all motion and no progress." However, there is yet hope that in the near future

some of the best features of the American system, as described by Mr. Cannon, may be copied by Canadian bankers, and there is also good reason to pray that we may always be spared the adoption of the method of settlement known in New York and elsewhere as "clearing-house certificates." The bankers of the Dominion would, we venture to think, in the light of their experience of 1893, when the requests for payments of balances due by New York banks to their Canadian correspondents were met with offers of clearing-house certificates, unite in declining to pronounce such useless attestations to the accuracy of the amount due to them as an equivalent for or representative of cash.

But since the amalgamation of the bankers' section of the Board of Trade with the Montreal clearing-house, the members of the united body have felt more free to prescribe rules and regulations, and to frame agreements for the control of the banks of Montreal in various matters. It is to their action that the officials employed in the banks owe their enjoyment of a genuine half-holiday every Saturday. The popularity of this movement has been attested to by the majority of the clearing-house cities of Canada, and by several of the monetary institutions at less important points. Nearly every banker in the Dominion has now the weekly opportunity of seeking health and recreation in the country during the summer months, and to devote an afternoon all the year round to athletic sports and exercise. Perhaps the success of their efforts in devising means of taking care of the health of their officials may spur bank managers into renewed effort to cope successfully with the many projects for united action upon all questions affecting their mutual welfare.

Mr. Cannon, in his history of clearing-houses refers to the development by every profession and trade of its own peculiar terms and phrases, and he states that the usage in this regard by banks and clearing-houses is no exception to the general rule. Of course, to those familiar with the routine work of a Canadian bank it will not be difficult to comprehend the current terms employed in describing the mechanism of a clearing-house. It will not be necessary to state that the term "to clear" means "to pass through the clearing-house." But it is a safe deduction in philosophy that what is a simple detail in the daily current of the lives of bank officials may be to their brothers as a Chinese laundry bill is to the man who is unacquainted with the monetary signs of the followers of Confucius. We, therefore,

deem it only fair to any one who has not attended the clearing-house, to quote Mr. Cannon's definition of the term "to clear."

"The term 'to clear' is popularly defined, to 'pass through the clearing-house.'" Another definition is "to settle accounts by exchange of bills and cheques as is done in the clearing-house." To clear a cheque means to pass it from the bank that holds it as a deposit or for collection to the bank on which it is drawn, and to receive payment therefor, but, with the complexities of modern business, a single cheque is seldom cleared. Instead, a multitude of cheques and other items are included in each clearing. The term "to clear" therefore takes on a broader meaning, and the only adequate conception of it is afforded by a view of the actual operations of a clearing-house, which are set forth in another part of this volume."

Having given Mr. Cannon's explanation of what a clearing-house between banks designates, we will now proceed with this brief history of the Montreal clearing-house, and endeavour to describe its mechanism, and the daily doings of its members. At the close of the year 1888, a small committee, composed of the senior officers of three of the leading banks, issued a circular giving a few practical reasons for the establishment of a clearing-house. In this circular, it was stated that the proposed clearing-house would only deal with the matter of clearings, and that the mechanism would be made as simple and concise as possible. Eventually the plan adopted was almost identical with the system of clearing so successfully introduced at Halifax, N. S., in the previous year.

The reasons advanced in 1888 for having a clearing-house in Montreal must appeal to every business man in Canada:—

- Time saved in daily exchanges and obtaining settlements.
- Diminution of risk to bank messengers delivering deposits.
- Prompt settlement of balances instead of vexatious delays.
- Less actual cash required in settling, having only one balance to pay or receive instead of a number.

Saving of time and labour in each bank, no bank ledger, bank pass books, nor bank entries in cash being necessary with the proposed system of clearing.

A meeting of the interested banks was held, a committee appointed to draft rules and regulations, and the Montreal clearing-house opened for the purpose of effecting the first exchange of cheques and notes between banks under the new system on January 7th, 1889, at a temporary room in the Merchants Bank of Canada.

Some of rules and regulations then adopted are still in force, and are found to work admirably. A committee of seven bank representatives appointed to manage the affairs of the clearing-house made arrangements with the Bank of Montreal to act as clearing bank for the receipt and disbursement of balances due to and by the various banks. Beyond some slight changes in the time of meeting, and the abolition of a second meeting each day to adjust differences owing to returned items, the following rules are yet in force, and form a fair outline of the daily course of procedure in exchanging and settlement between the banks of the chief city of Canada.

"The clearing bank shall be responsible only for the sums of money actually received by it from the debtor banks and for the distribution of such sums among the creditor banks on the presentation of the usual clearing-house certificate properly discharged. The clearing bank to give the usual receipt for balances received from the debtor banks. The board of clearing shall also arrange for an officer to act as manager of the clearing from time to time.

"The hour for making exchanges at the clearing-house shall be ten o'clock a.m. precisely. All debit balances must be paid into the clearing bank between twelve and twelve-thirty o'clock of same day, and between 12.30 and 1 o'clock p.m. the creditor banks shall receive from the clearing bank the balances due to them respectively, provided that the balances due from the debtor banks shall then have been paid. But on no condition shall any creditor balance or portion thereof be paid until such debtor balances have been settled. The medium to be used in clearing shall be legal tenders of the largest possible denomination.

"In the event of any bank failing to pay the balance against it at the proper hour, such bank shall be ruled out by default and notice thereof in writing given by the manager or cashier of the clearing bank to the other banks. The amount of said balance shall be supplied to the clearing bank by the members to whom the defaulting bank is a debtor in proportion to the amounts due to them respectively from the defaulting bank according to the exchanges of that day. After the clearing, the respective amounts so supplied to the clearing bank on account of the defaulting bank will constitute claims on the part of the responding banks against the defaulting bank. Any such responding bank may cancel its exchanges of the day with the defaulting bank by tendering repayment to said defaulting bank of the amount, if any, of cheques and other

items received by it (the creditor bank) through the exchanges of the day at the clearing-house from or on account of the said defaulting bank, and receiving in return all the cheques and other items delivered by it to the defaulting bank in the morning exchanges at the clearing-house of the day on which said default occurred.

"Errors in the exchanges and claims arising from the return of cheques or from any other cause are not to be adjusted through the clearing bank but directly between the banks interested."

We have referred to the first meeting of the Montreal clearing-house. The results of the clearing on that occasion are recorded in the minute book of that body with pardonable pride in the success of the venture. The clearing-house proved to be all that had been claimed for it as a time and labour-saving device. The exchanging of parcels commenced at 10.10 a.m., the total amount delivered by the sixteen banks in attendance being \$1,458,474.84. The amount of money required under the new system to be paid into and disbursed by the settling bank was only \$390,452.06, and the time consumed by the clerks and officials in effecting this exchange was fifty minutes. Under the old plan of bank to bank delivery, fully one half of a banking day would have been given to arriving at the same goal.

The passage of time has much more conclusively exhibited the incalculable advantages of the clearing-house as a means of effecting the daily exchanges of notes and cheques between banks. The record day's clearing of the present year in Montreal amounted to \$8,392,236 the actual sum in legal tender notes required in settlement was \$1,300,000 and the actual time required in delivering, receiving and balancing was only 15 minutes.

Such facts and figures as these clearly demonstrate the extreme usefulness, and in the illustration just given they do more. They show the expansion of the trade and commerce of the country since the year 1889, even if it has to be admitted that a large percentage of the 8½ millions of dollars referred to as a day's clearing in Montreal in November last represented the receipts of the stock exchange.

The table published herewith has been carefully compiled from the records of the Montreal clearing-house, and exhibits the annual increase in the amount of money annually passing through the clearing-house of the metropolis.

1899.....	\$794,029,000
1900.....	\$730,933,000
1901.....	\$889,479,000
1902.....	\$1,098,970,000
1903.....	\$1,113,978,000
1904.....	\$1,065,067,000
1905.....	\$1,324,313,000
1906.....	\$1,533,597,000
1907.....	\$1,555,729,000
1908.....	\$1,467,316,000

What takes place at the meetings in Montreal of the banks' representatives for the purposes outlined in this brief history may be summarized thus:—

The exchange occurs daily at 10 o'clock a.m. (on Saturdays half an hour earlier). Each bank, at the appointed time, sends representatives to the clearing-house with the notes and cheques of other banks enclosed in sealed envelopes.

At the appointed time, the manager calls out "ready"! and rings a bell. Each messenger from the eighteen banks then delivers the parcels in his possession, and receives in return other parcels and returns to his respective bank with his delivery statement duly initialled by the clerks who have received the parcels he has delivered. The clerks remain to transcribe the amounts received as shown by tickets removed from the parcels delivered to their respective messengers to settling sheets, and proceed to calculate the difference between the amounts delivered and the amounts received—the said differences constituting the debit or credit balance for which the manager of the clearing-house, if his figures agree with their claims upon him, signs vouchers to be used later at the settling bank. If the work of those present has been performed with accuracy, and the manager finds from the vouchers delivered to him that the amounts therein stated as due to the clearing-house exactly agree with the amounts due by same, the satisfactory result is announced by another ringing of the bell, and the attendant clerks return to their respective banks.

A careless or incompetent official may cause confusion and delay, and necessitate a search for errors varying from one cent to one hundred thousand dollars. However, a discrepancy seldom remains long undiscovered, and, when the error is traced to its source, the culprit is presented by the manager with a valentine, in the shape of a card, inviting the recipient

to pay a fine to the treasurer. The following notice, conspicuously displayed in the clearing room, shows the fines to be moderate in amount. Since the imposition of penalties about six months ago, there has been a marked improvement in the work performed by those who attend at the Montreal clearing-house. The rules and fines read as follows:—

"Representatives of banks in attendance at the clearing-house will be required to conduct themselves in a quiet and orderly manner, be attentive to their duties, to remain at their desks while the proof is being made, and until it is announced. Loud communications, conversation, or anything tending to create disturbance or confusion, will not be permitted.

"All fines imposed by the manager will be paid to the treasurer at once.

"The manager is authorized to require from members, the signatures of those authorized to sign receipts for balances.

#### FINES.

1. All errors on the credit side (amount brought) of settling clerk's statement ..... \$0 50
2. Errors in making debit (amount received) entries.... 50
3. Errors in tickets on parcels causing disagreement between balances and the aggregate ..... 50
4. Errors in addition of amount received by bank..... 1 00
5. Disorderly conduct of clerk or delivery messenger at the clearing house; or disregard of manager's instructions, each offence ..... 2 00
6. Clerk or messenger failing to attend punctually at the morning exchange ..... 1 00
7. Debtor banks failing to appear to pay their balances at the time appointed at the settling bank..... 5 00
8. For all errors remaining undiscovered at eleven o'clock fines will be doubled."

Should errors be discovered in the sealed packages referred to, the differences are adjusted between the interested banks without having recourse to the clearing-house.

As the fine for failure on the part of the bank's representatives to attend punctually when first introduced occasionally led to an exchange of opinions about the veracity of the clearing-house clock, the following notice is posted in the clearing-house where all concerned may read and digest same:—

Any representative of a bank, desirous of questioning the time as told by the clearing-house clock, will kindly report his

wish *immediately on arrival* to the presiding officer, so that the correct time may be promptly ascertained by telephone and the clearing house clock regulated, if necessary.

As a "perfect and satisfactory settlement of the daily balances" between their members, the clearing-houses established in Canada have been notably successful, and the founders thereof probably never intended that the functions of a clearing-house should include aught else than a daily meeting for the purpose of effecting an exchange of cheques and notes.

To quote again from Mr. Cannon's history:—

"No uniform rates of charges for collection of items, no maximum rates of interest on deposits, no borrowing and loaning of balances at the clearing-house, no procuring of legislation relative to banking, no clearing house loan certificates, and no bracing up of weak members are known to the Canadian Clearing House Associations. It has been left to the Canadian Bankers' Association to do whatever is possible in securing proper legislation for the banks. The necessity for the issue of clearing-house certificates in the United States, as shown in another chapter, has been due, in the main, to the lack of elasticity in our currency, and *since the banking issue in Canada obviates this weakness, there has been no occasion for the issue of such certificates.*"

Mr. Cannon claims that the American clearing-house system was not borrowed from that of any other country, but that it is *possible* that some of those who were responsible for the organization of the first clearing-house in America "knew somewhat of the existence of a clearing-house in London." We do not regret that this is as it is. We are glad to think that Mr. Cannon found the origin of the London Clearing House to be shrouded in doubt and uncertainty. We subscribe to his belief that the clearing-house is a "growth or development something proceeding from well-defined causes and springing into existence to meet a clearly expressed want." He adds, "It was presumably at the outset an institution of so little importance that the historians of the day paid no attention to it." Be this as it may. There is record in the books of Martin & Co., Bankers of London, in 1773, of payment of 19s. 6d. for a quarter's rent of the clearing-room. (See Mr. Cannon's book.)

The admission of the historian of clearing-houses that he found the origin of the London institution shrouded in doubt and uncertainty inclines us to pin our faith to the old, old,

story of its birth told by English bankers, and to believe that a few of the wide awake forefathers of the present race of bank messengers found their daily work could be materially reduced by meeting at one of the central London coffee-houses, and there, over a pint pewter of ale, exchanging the parcels they would otherwise have had to deliver from bank to bank.

To a reflective mind, the changes which have occurred since these unknown founders of the first clearing house endeavored to simplify and facilitate the work of banks are surprising. The London coffee-house and the messengers of 1773 have passed away, and the revolutions of years have given us patatial, edifices, like the New York Clearing-House, and a steady, well-conducted set of men in the neat and simple uniforms of their respective banks, with a quiet, thorough-going way of passing along to their duty at the clearing-house without regard to the allurements of the modern coffee-house.

The clearing-house is one of the many ingenious devices to simplify and facilitate daily work, the privation of any one of which would grievously disturb the temper and affect the comforts of the present generation.