The Life and Legacy of the Second Bank of the United States

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Overview

- Early in its history, Congress twice granted charters for quasi-public yet privately operated banks. The first time was in 1791, shortly after ratification of the U.S. Constitution, and the second in 1816, following the War of 1812. Both received 20-year charters, and both went un-renewed.

- The “First” and “Second” Banks of the U.S. were fiscal agents to the Treasury, and established branches around the country to hold government deposits and to make payments. In this sense they were private banks serving the public interest. Whether private or public objectives took priority, however, was at the center of controversies surrounding their existence.

- The 1st and 2nd BUS made commercial and private loans with the government’s surplus balances and regularly paid large dividends to private shareholders. In this sense they were very “private” banks.

The First BUS

- By most accounts, including even its early opponent Thomas Jefferson, the Bank served the Treasury well, and funded projects that helped the nation build much of its early infrastructure (Rousseau and Sylla 2005).

- Opposition usually focused on questions of constitutionality. Alexander Hamilton, the first Treasury Secretary, broadly interpreted Article 1, Section 8 of the Constitution, which reserves to Congress the right to “coin money and regulate the value thereof” through any means “necessary and proper,” as justification for creating a mint and federal bank.

- Congress approved the charter, but it was not until after the Second Bank was formed that the Supreme Court confirmed its constitutionality in 1819 and again in 1824.

- The Bank regularly paid annual dividends of eight percent to its shareholders, which critics viewed as excessive and used to fan the flames of its failed recharter in 1811.

The Second BUS: Early Days

- The Second Bank was intended to remedy financial problems faced during the War of 1812, when there was no federal bank, but quickly deteriorated into making large loans to insiders, coming close to bankruptcy within two years under its first President, William Jones.

- Successor Langdon Cheves was more able, yet contracted loans sharply when a financial panic took hold in 1819. Some claimed that the Bank had saved its shareholders at the expense of the public.

- When Nicholas Biddle takes over as the Bank's President in 1823, the situation seems to turn around. Biddle took pride in conducting the government's business efficiently and monitoring banks' note issues, while still lending out the public surplus to provide robust returns to shareholders.

The election of Andrew Jackson in 1828 was a sea change. He fires the opening salvo in December 1829:

“The charter of the Bank of the United States expires in 1836, and its stock holders will most probably apply for a renewal of their privileges. In order to avoid the evils resulting from precipitancy in a measure involving such important principles and such deep pecuniary interests, I feel that I cannot, in justice to the parties interested, too soon present it to the deliberate consideration of the Legislature and the people. Both the constitutionality and the expediency of the law creating this bank are well questioned by a large portion of our fellow citizens, and it must be admitted by all that it has failed in the great end of establishing a uniform and sound currency” (First Annual Message to Congress, 8 December 1829).

A year later, Jackson’s message to Congress is more conciliatory:

- *“In the spirit of improvement and compromise which distinguishes our country and its institutions it becomes us to inquire whether it not be possible to secure the advantages afforded by the present bank through the agency of a Bank of the United States so modified in its principles and structure as to obviate constitutional and other objections” (Second Annual Message, December 6, 1830).*

- Biddle takes these words seriously, believing that Jackson would develop a kinder view of the Bank with time. He works through Secretary of State, Edward Livingston, who lists conditions for renewal in early 1832. These appear to have been:

1) Government to have no interest in the bank;

2) President of the US empowered to appoint a Director at each branch so that government may be represented at each;

3) States authorized to tax the property both real and personal of the bank within the said States in like manner as the States may tax other property within them;

4) Bank hold no real Estate but such as it may be constrained to take in payment or security of its debts, and to be compelled by law to sell that within a stated time.

Two other terms were specified by the President’s advisors, but supposedly not from Jackson himself. These were

5) a certain proportion of the stock or capital to be thrown open to new subscriptions, which may be done by prorate reduction of the present capital, or by addition to it, and

6) the Directors to nominate annually two or three persons of whom the (U.S.) President to appoint any one as *President of the Bank*.

(Ingersoll to Biddle, 23 February 1832).

Biddle seems satisfied with these events, writing to Ingersoll:

> *"In truth I believe there is no change desired by the President which would not be immediately assented to by the Bank. And this it is which gives me so much regret, to find the President and the Bank apparently estranged while there is really no difference between them, and to see the President's friends lose the present opportunity of settling the question so well, and so advantageously for them" (Biddle to Ingersoll, 26 February 1832).*

The Veto

- Shortly after this, Jackson’s advisors convince Congress to conduct an investigation into the Bank’s affairs, which delays action on the Bank until its completion in May 1832.

- Biddle makes no concessions to the President in the final bill, and one can only suspect that Clay had a hand in turning the Bank into a political issue. As brought to the President’s desk, it is therefore unsurprising that Jackson vetoed it on July 10, 1832.

- Biddle is slow to realize the defeat, and a private letter to Clay a month after the veto indicates a belief that he still had the upper hand.

"As to the Veto message I am delighted with it. It as all the fury of a chained panther biting the bars of his cage. It is really a manifesto of anarchy – such as Marat or Robespierre might have issued to the mob of the faubourg St. Antoine: and my hope is that it will contribute to relieve the country from the dominion of these miserable people. You are destined to be the instrument of that deliverance, and at no point of your life has the country ever had a deeper stake in you." (Biddle to Clay, 1 August 1832).

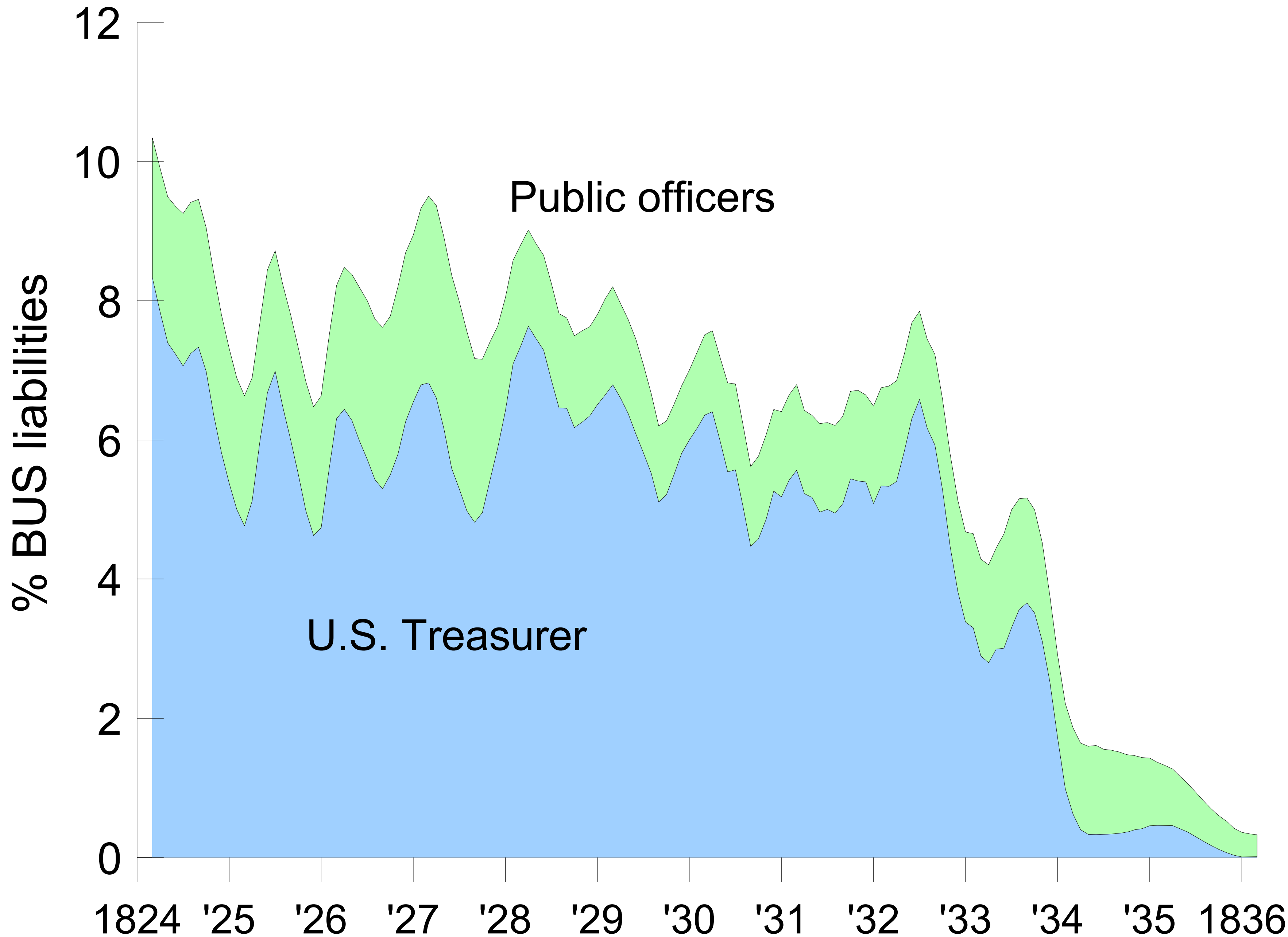
- In pressing the re-charter decision before the election either to force the President's hand or make him look foolish, Clay miscalculates the strength of populist support for Jackson, and loses the general election to him in a landslide defeat.

The “Bank War”

- Upon re-election, Jackson escalates the campaign against the Bank, citing the degree of private control wielded by the nation’s fiscal agent and charging it with failing to provide a “sound and stable currency.”

- Sec. 20 of the Act of Incorporation: “*The deposits of the money of the United States in places in which the said Bank and Branches thereof may be established, shall be made in said Bank, unless the Secretary of the Treasury shall otherwise order and direct; in which case the Secretary of the Treasury shall immediately lay before Congress, if in session, and if not, immediately after the commencement of the session, the reasons of such order and direction.”*

- Biddle interprets Sec. 20 as authorizing the Secretary to remove deposits if mismanagement presents a threat to their safety, which he does not believe, yet the Congress form a committee in 1832 to investigate exactly this.



% BUS liabilities
0
2
4
6
8
10
12
Public officers
U.S. Treasurer
1824
'25
'26
'27
'28
'29
'30
'31
'32
'33
'34
'35
1836

- The inquiry concludes that the deposits are safe, but later while Congress is adjourned Jackson proceeds to fire two Treasury Secretaries until Roger Taney orders the removal of the deposits, citing "reason to believe that the charter had been violated."

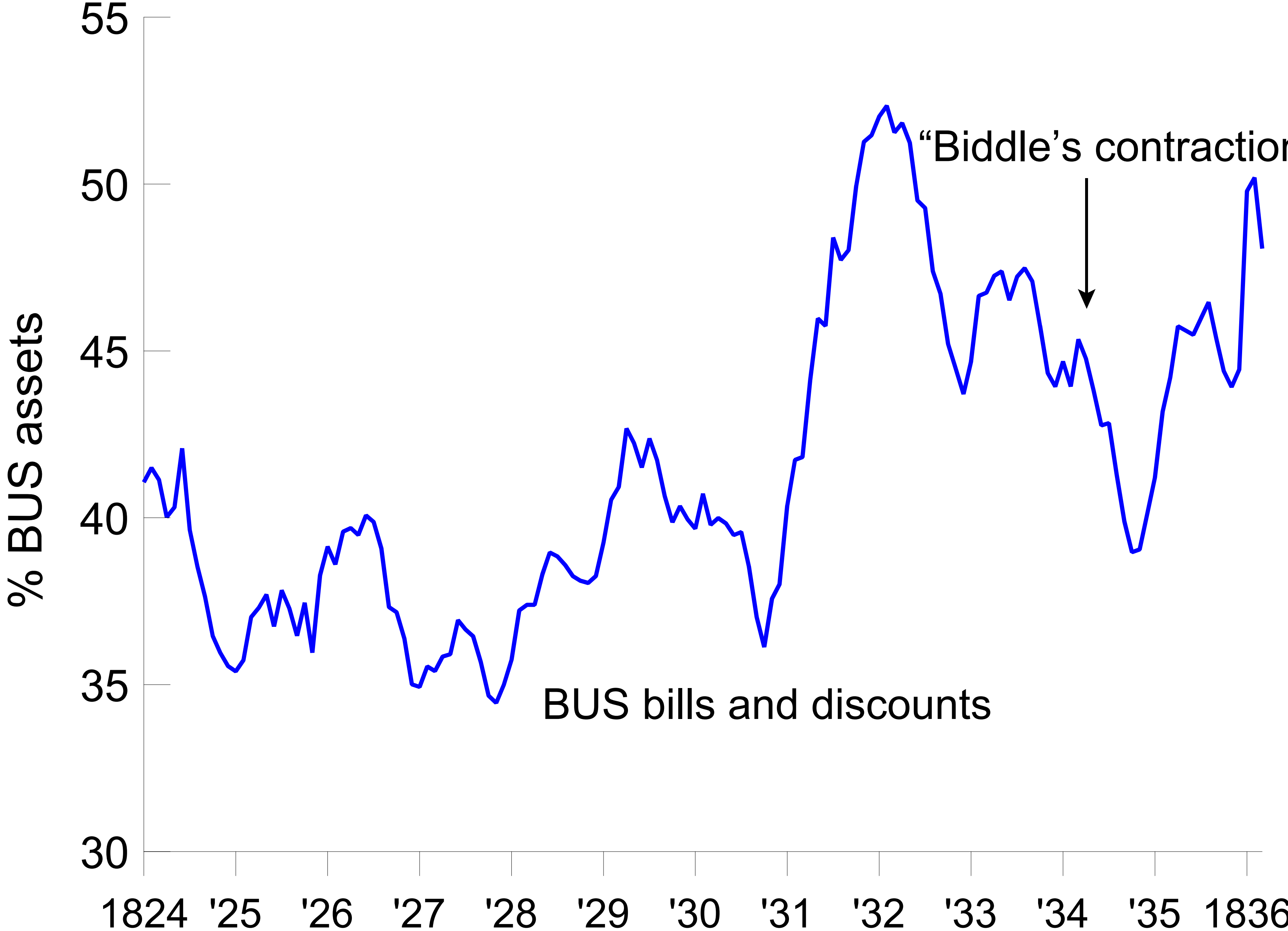
- With the deposits removed, Biddle acts as if released from the responsibility of monitoring other banks and controlling the nation's credit.

- Biddle summarizes this view in an early 1834 letter to the Judge of the U.S. Court in the Eastern District of Pennsylvania:

"You may rely upon it that the Bank has taken its final course and that it will be neither frightened nor cajoled from its duty by any small driveling about relief to the country. All that you have heard on that subject from New York is wholly without foundation. The relief, to be useful or permanent, must come from Congress and from Congress alone. If that body will do its duty, relief will come – if not, the Bank feels no vocation to redress the wrongs inflicted by these miserable people. Rely upon that. This worthy President thinks that because he has scalped Indians and imprisoned Judges, he is to have his way with the Bank. He is mistaken – and he may as well send at once and engage lodgings in Arabia…" (Biddle to Hopkinson, 21 February 1834).

- He expresses a more reserved sentiment in a letter to Cincinnati lawyer and journalist Charles Hammond:

“The deposit banks being now in full possession of the public revenue may employ it in discounts and leave the Bank of the United States the opportunity of gently diminishing its business. That with so wide a circulation as 18 or 19 millions which the receipts of the public revenue may place in the hands of officers who know that no service more acceptable can be rendered than to employ the funds in injuring the Bank, and so many vulnerable points to protect, we shall deem it expedient to reduce the present amount of our loans, cannot be doubted. The Executive, by removing the public revenues has relieved the Bank from all responsibility for the currency, and imposed upon it a necessity to look primarily to the interests of the Stockholders committed to our charge” (Biddle to Hammond, 11 March 1834).


% BUS assets
55
50
45
40
35
30
1824
'25
'26
'27
'28
'29
'30
'31
'32
'33
'34
'35
1836
“Biddle’s contraction”
BUS bills and discounts

The Path of Destruction Leads through New York

- Earliest indications of the Bank falling out of favor in New York come from votes in State Assembly 6 April and 9 April 1831 on “resolved, that it is the sentiment of this legislature, that the charter of the BUS ought not be renewed.” Defeated on 6 April by vote of 55-55 with the New York City reps voting 8-1 in favor of the Bank.
- When the resolution is called for a second vote on 9 April, four positive NYC reps are absent and two anti-Bank legislators not present on 6 April appear, ending in a 4-3 vote in favor of the Bank. Sentiment in other eastern counties see complete reversals, delivering statewide vote of 71-35 against the Bank.
- When re-charter Bill is brought to a vote in Congress on July 3, 1832, the New York delegation votes12-19 against the Bank in the House and 0-2 against in the Senate, despite the Northeast and Middle Atlantic being generally supportive and the Bill carrying by overall votes of 107-86 in the House and 28-20 in the Senate.

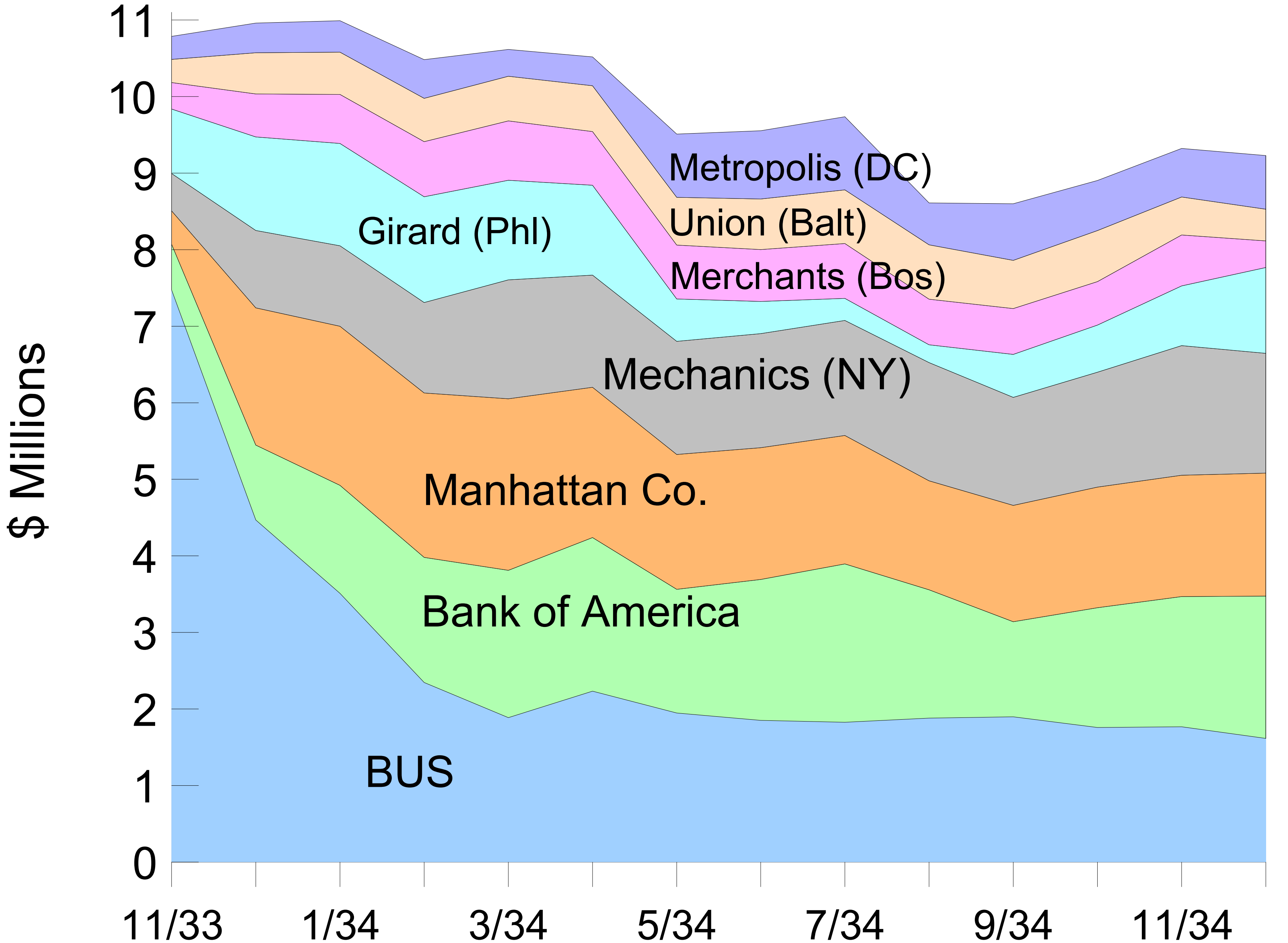
- The key economic question for Jackson leading up to the removal is where to lodge the deposits and which state banks would act as fiscal agents.
- The plan requires the enlistment of major banks in the Eastern cities as new depositories, with New York as the lynchpin.
- Shortly after Congress adjourns for Summer in 1833, Jackson sends Amos Kendall (“Kitchen Cabinet”) through Baltimore, Philadelphia, New York, and Boston to inquire whether the larger State Banks would assist the gov’t in its business were the need to arise. Kendall was under orders not to inform these bankers about the possible removal as this would reveal Jackson’s hand.
- Kendall receives little positive news from the New York at first, with many fearing retribution from BUS, but is received favorably at the Bank of America, where every director is a Whig!

- To quote from Kendall's autobiography:

The president, Mr. Newbold, was a gentleman of comprehensive views, who did not accept the dogma of his party that a national bank was a necessary fiscal agent of the government, and he fully appreciated the wrong done to New York in depriving her of her natural advantages by the legislation of Congress, which undertook to make Philadelphia the financial centre of the Union. He also was sagacious enough to see that the gratuitous transfer of the public monies, which was a bugbear to other banks, could be made a source of profit instead of loss (Kendall, 1872, 381).

- Apparently greed and resentment of the power amassed by the Philadelphia institution and its access to public deposits was stronger than political ties could hold in check. When calling upon the Democrat-controlled Mechanics' Bank of New York on the return trip, Kendall recalls expressing regret that

  A bank on which the administration had relied in this emergency as one controlled by his friends, should reject the benefits to be derived from the government agency, particularly as the Bank of America had already acceded to the terms proposed." He (i.e., Kendall) appealed to the president to call his board together and reconsider the subject. That official did so, and twenty-four hours afterwards handed in another document acceding fully to the terms proposed. The Manhattan Company, which had thus far held back, now came forward and accepted in full the proposed terms (Kendall, 1872, 381).



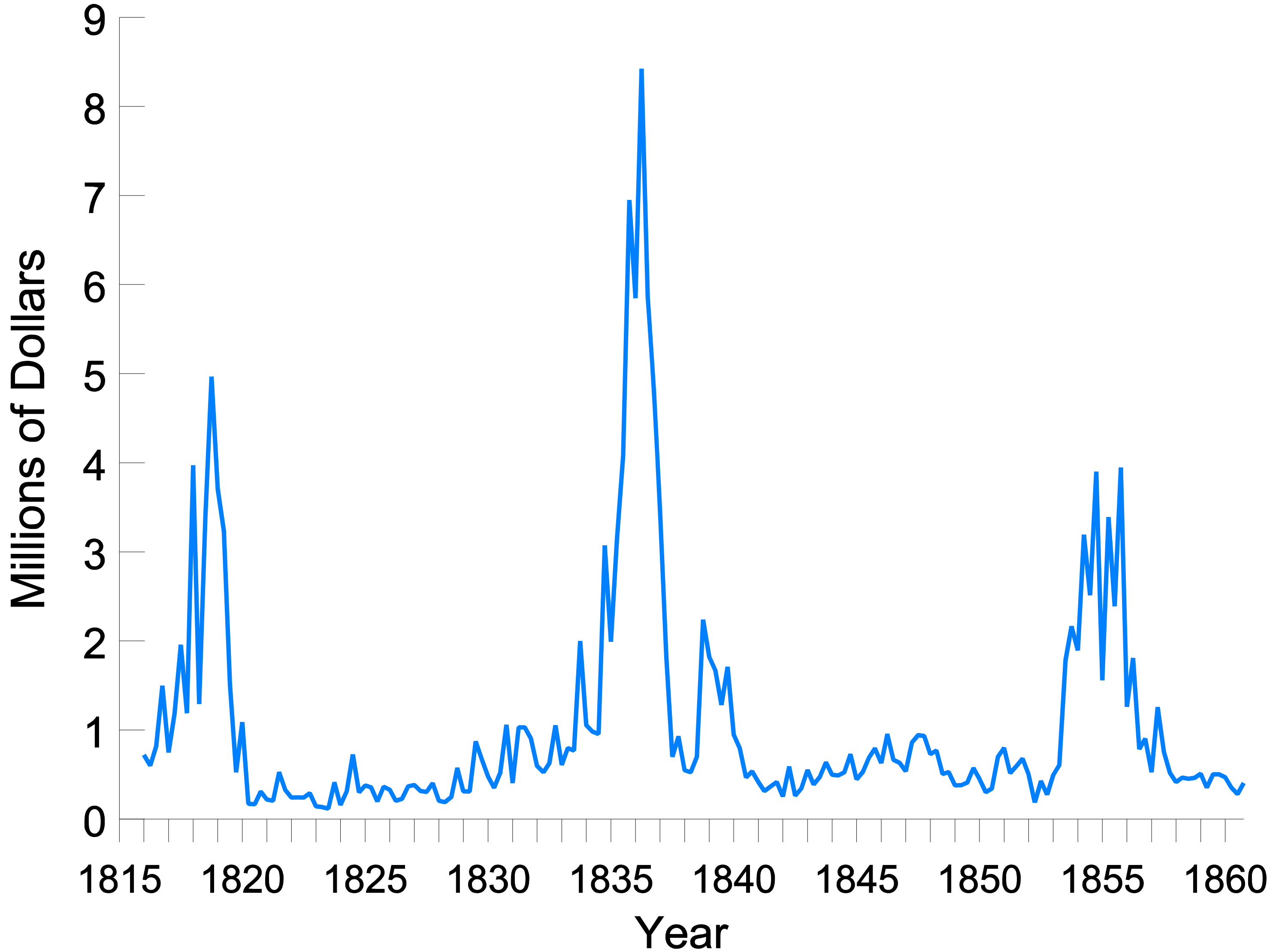
11
10
9
8
7
6
5
4
3
2
1
0
$ Millions
Metropolis (DC)
Union (Balt)
Merchants (Bos)
Girard (Phl)
Mechanics (NY)
Manhattan Co.
Bank of America
BUS
11/33
1/34
3/34
5/34
7/34
9/34
11/34

The Panic of 1837 and its Aftermath

- The Secretary distributes the deposits among additional “pet banks” throughout the country, hastily selected by Jackson democrats. These bankers multiply their new base money, which along with specie flows from Mexico and points south intensify a mounting inflation.

- A boom in sales of public lands in the new “west” and “southwest” leads Jackson to issue an executive order (the “Specie Circular) in June 1836 requiring all public lands be paid for with gold or silver coins. This does not slow land sales, but rather drains gold and silver reserves from eastern banks to the west.

- With the nation’s federal debt paid off in 1835, surpluses from customs and land sales accumulate in the pet banks, especially in New York City. This leads the Jackson Democrats to pass a “Deposit Act” in 1836, which called for a “Distribution of the Surplus” back to the states in accordance with their population beginning in 1837. This further drains eastern reserves.



Quarterly Public Land Sales, 1816-1861

- These measures combine with balance of payments deficits to bring public fear and launch bank runs in New York on May 10, 1837. In a weakened condition, the banks there suspend convertibility of their notes into coin, and this propagates into the nation’s first general suspension. A recession ensues for the next six years, and the nation goes without a federally-chartered bank until December 1913, when the Federal Reserve Act is passed.

A Third BUS?

- In August 1841, Whigs led by Clay passed a bill through both houses of Congress authorizing a new federal bank and fiscal agent, called the “National Bank of Issues.”

- The proposed bank would have capital of $30 million,$5 million less than the Second BUS, would have 1/3 ownership by the government, and would have dividends capped at 7% per annum. Congress could terminate its otherwise 20-year charter in 1846.

- Former Democrat and recently-turned Whig John Tyler, who had ascended to the Presidency four months earlier, vetoed the bill on September 9. The veto message raised constitutional questions, noted that exchange bills could be used for accommodation, and expressed concern that there were no limits on the premia the bank could command on bills.

- In most substantive respects, the “Third” Bank would have been like the Second.

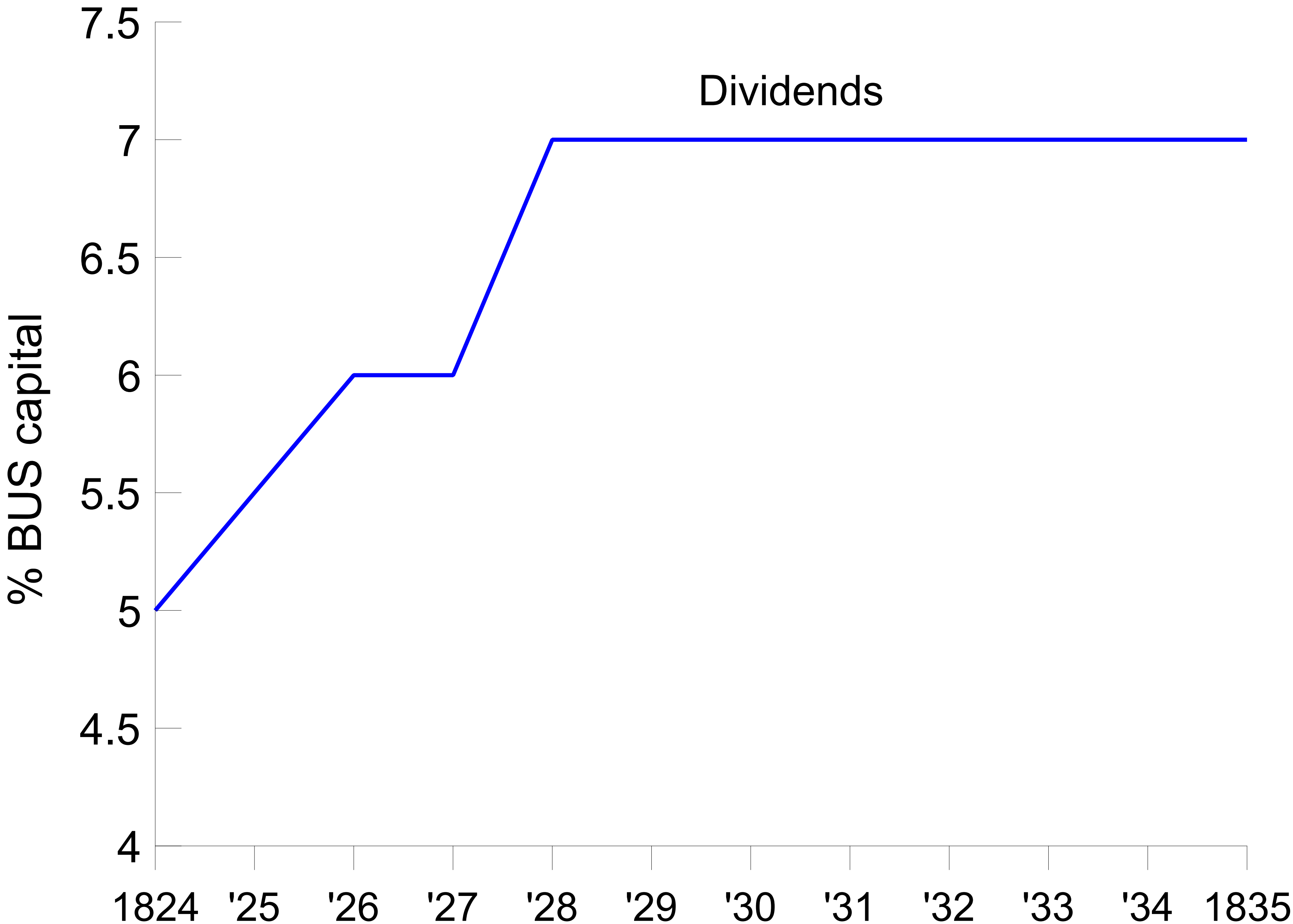
What can be learned from the Second Bank?

- What Jackson sought was greater public accountability and oversight for the privately-controlled federal bank. The Secretary could provide some, but was not directly involved in the Bank's governance. Biddle seemed benevolently at the helm of the nation's monetary affairs, yet shareholder distributions seemed to have priority. Even if this were acceptable, would every Bank President take the public role as responsibly as Biddle?

- Jackson was not the first to notice the deficiency, but the one who acted most strongly upon it.

- Of course, the Bank was distributing $2.45 million each year in dividends at a time when GDP was about $1 billion and per capita income was about $100. Jackson could never articulate well his opposition to the Bank or a vision for a replacement, and charter-based arguments against the Bank always seemed weak.

Jackson slaying the multi-headed hydra…

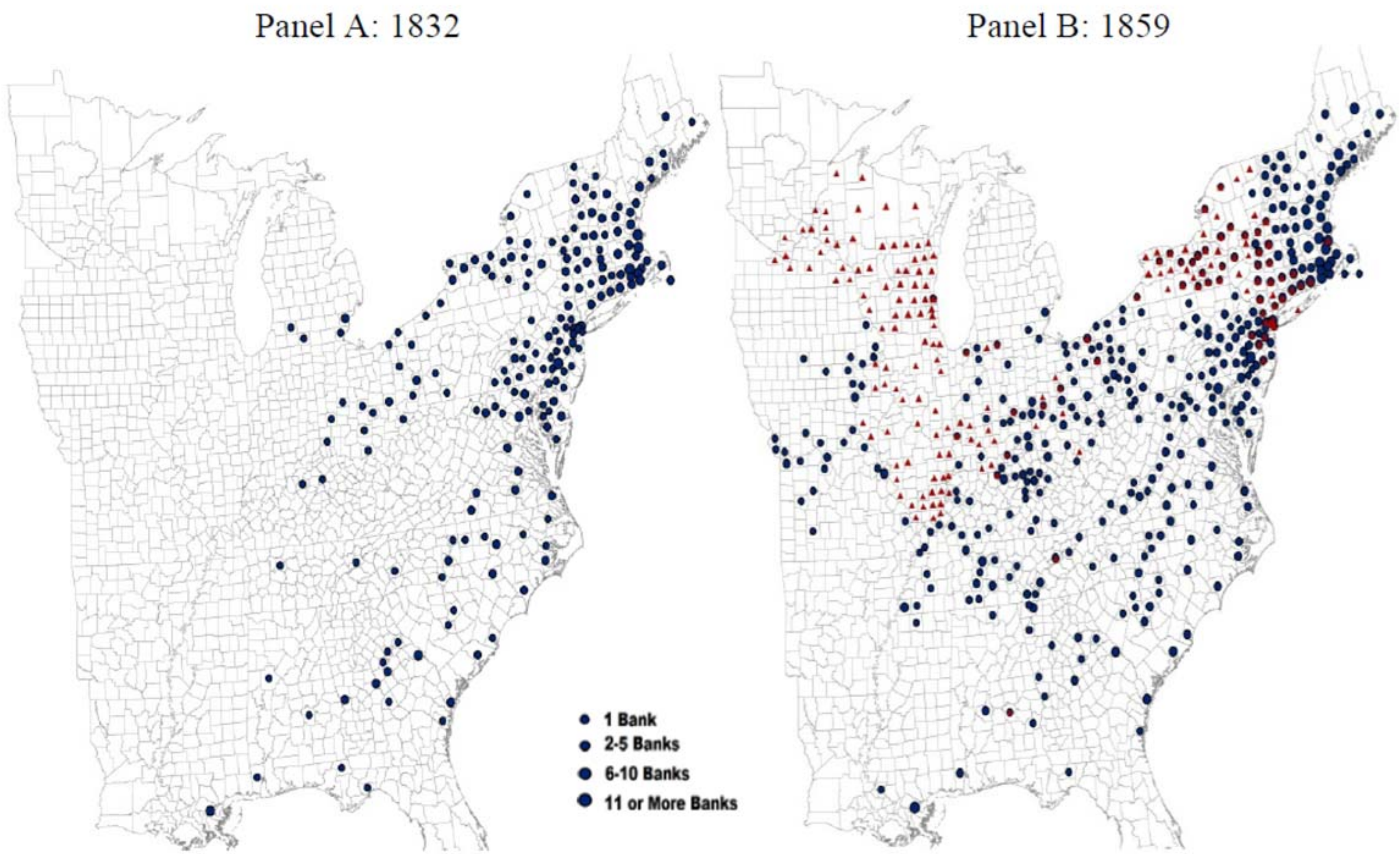


Dividends
% BUS capital
7.5
7
6.5
6
5.5
5
4.5
4
1824
'25
'26
'27
'28
'29
'30
'31
'32
'33
'34
1835

- Though short term effects of the Bank War were severe, it is possible to take a more positive view of Jackson's moves in the long-run. The free banking movement allowed the system of banks to expand, and the National Banking System furthered this, while also demonstrating the dangers of an inelastic currency.

- Even Bray Hammond (1936, 184), a sharp critic of Jackson policies, concedes that:

  "Free banking is a direct heritage from Jacksonian democracy. The interest of Jackson himself in banking was mainly destructive, but the people who gave him his following – the mass of rugged individualists imbued with what Gallatin called with dismay the fierce spirit of enterprise – wanted not to stop with the destruction of the Bank of the United States, but beginning with that to erect thousands of local banks owned by local capitalists. They wanted to destroy the monopoly and make banking open to all."



The Distribution of Free and Charter Banks, 1832 and 1859.

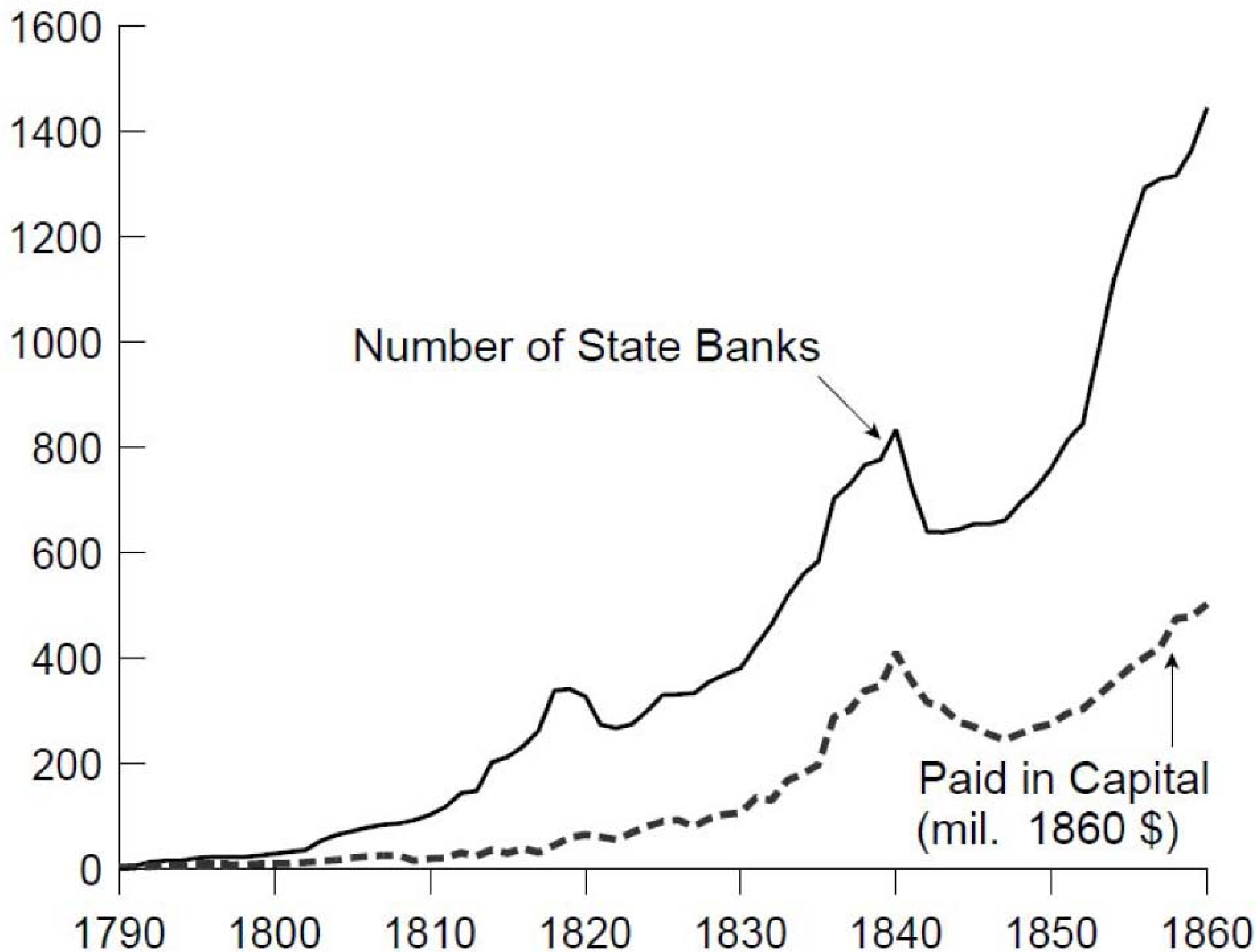


Figure 1. Number of Banks and Aggregate Paid-in Capital, United States 1790-1860.

- The Second Bank showed that concentration of monetary interests in the hands of a few tended to constrict the banking system. Though banks would likely have expanded in any case, we cannot know how quickly had the Second Bank survived. Yet the expansion did round out the banking map, leaving a footprint that the Federal Reserve inherited upon its founding.