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# Judicial Comment On The Concept of “Banking Business”

C. C. JOHNSTON\*

Section 75(1) of Canada's Bank Act lists activities which banks may perform. The first four subsections refer to specific activities, but 75(1) (e) is a broad provision which states that banks may “engage in and carry on such business generally as appertains to the business of banking.” The purpose of this article will be to examine the concept of “banking business” in the light of judicial interpretation.<sup>1</sup> One approaches the task with a considerable degree of humility, for as Chorley has said in his book on banking, “to construct a definition which would embrace the whole of it is manifestly impossible”.<sup>2</sup>

The difficulty is increased by the fact that banking, like other forms of business, continues to develop and expand its activities to meet its competitors and provide wider services for the public with the result that any attempt to squeeze the concept into the confines of a definition may prove successful today but inadequate tomorrow. A further obstacle to definition is the fact that forms of banking have frequently been carried on in conjunction with other businesses and are occasionally so inextricably woven in with these that it is difficult to isolate the purely banking activities. In other words, the concept becomes coloured by its close association with other forms of business and it is sometimes problematical whether a specified activity is an incident of banking or of some other business. An example of this intermingling of activities is provided by the loan and trust companies which carry on certain activities remarkably similar to those of banking. Such companies take money on deposit, issue passbooks, pay cheques drawn on these deposits and make loans on certain securities specified by statute.<sup>3</sup>

In England, as Chorley points out, the discussion of what exactly constitutes banking business has become largely academic because of

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<sup>1</sup> “The nature of the business of bankers is a part of the law merchant and is to be judicially noticed by the Court.”—per Lord Campbell in *Bank of Australasia v. Breillat* (1847) 6 Moo. P.C. 152 at 173, 13 E.R. 642 at 650.

<sup>2</sup> Chorley, *Law of Banking*, 4th ed. 23.

<sup>3</sup> *Trust Companies Act*, R.S.C. 1952, c. 272, sec. 64 (1) (c) & (d).

*Loan and Trust Corporations Act*, R.S.O. 1960, c. 222, sec. 139(4).

the concentration of most of the country's banking in a few great institutions.<sup>4</sup> In Canada, however, the subject is of more practical importance because of the division of legislative powers peculiar to the British North America Act. By section 91 (15) of the Act, the Parliament of Canada is given exclusive legislative authority over banking,<sup>5</sup> the incorporation of banks and the issue of paper money. Such authority has manifested itself in the Bank Act. If a business carries on activities which may properly be described as "banking",<sup>6</sup> then such a business should be subject to this federal power and, in particular, to such legislation as the Bank Act. Thus, if the loan and trust companies, for example, are carrying on what is in fact a banking business, they should come under the sway of the federal enactments. Moreover, since the powers in section 91 are exclusive, any provincial legislation purporting to regulate banking is "ultra vires"<sup>7</sup> and it is perhaps arguable that an act such as Ontario's Loan and Trust Corporations Act<sup>8</sup> is "ultra vires" in so far as it relates to banking activities.

How, then, have the courts determined what is banking business? The judges, of course, have not defined the concept for their own academic pleasure, but have done so in an attempt to create a standard for comparative purposes. Usually the purpose has been to decide whether a business should come within the authority of particular banking laws. A survey of the cases reveals three main approaches to creating such a standard or test. The first is a comprehensive listing of all the functions performed by bankers. This is an absolute standard and any business falling short of it is not a banking business in the fullest sense. The second is a less demanding test which contents itself with a majority of the more important activities carried on by banks. A complicating factor in this second approach arises where a business combines banking with other forms of enterprise. In this situation, the courts have used a balancing process to determine whether banking is incidental to or forms the major portion of the business.<sup>9</sup> The third approach is the lowest common denominator test which uses the key activities adjudged by the court to comprise the very core of banking. Such a standard has extremely wide application. As is readily seen, all three of these approaches have their drawbacks. The first is too rigorous, the second too uncertain and the third too elastic.

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<sup>4</sup> Chorley, *op. cit.* 24.

<sup>5</sup> The meaning of the term should not be restricted to banking as it was at the time the Act was passed. See *A.G. Alta. v. A.G. Can.* (Ref. re Alta. Bill of Rights Act), [1947] A.C. 503, Viscount Simon at 516; also, [1947] 4 D.L.R. 1 at 9.

<sup>6</sup> The federal banking power is "wide enough to embrace every transaction coming within the legitimate business of a banker." per Lord Watson in *Tennant v. Union Bank of Canada*, [1894] A.C. 31 at 46.

<sup>7</sup> See *A.G. Alta. v. A.G. Can.*, [1939] A.C. 117; *A.G. Can. v. A.G. Quebec*, [1947] A.C. 33, [1947] 1 D.L.R. 81, [1946] 3 W.W.R. 659.

<sup>8</sup> *Op. cit.*

<sup>9</sup> See *Stafford v. Henry* (1849) 12 Ir. Equity 400; *In Re Guinness* 1 I.R. Jur. 359.

Attempts to formulate a comprehensive definition may be illustrated by three examples drawn from English, American and Canadian law respectively. In England, a description of banking embodied in a statute states that,

'Banking business' means receiving money on current account or deposit; accepting bills of exchange; making, discounting, buying, selling, collecting or dealing in bills of exchange, promissory notes and drafts whether negotiable or not, buying, selling or collecting coupons; buying or selling foreign exchange by cable transfer or otherwise; issuing for subscription or purchase or underwriting the issue of loans, shares or securities; making or negotiating loans for commercial or industrial objects; or granting and issuing letters of credit and circular notes: except in so far as such operations form part of and are for the purpose of and incidental to the conduct of a business carried on for other purposes by the company, firm or individual by whom such operations are transacted.<sup>10</sup>

The definition which we find in *Corpus Juris Secundus* combines both the first and third standards.

Banking is the business or employment of a bank or banker, and as defined by law and custom consists of receiving deposits payable on demand, discounting commercial paper, making loans of money on collateral security, issuing notes payable on demand and intended to circulate as money, collecting notes or drafts deposited, buying and selling bills of exchange, negotiating loans and dealing in negotiable securities. . . . It is said, however, that any person engaged in the business carried on by banks of deposit, of discount or of circulation is doing a banking business although but one of these functions is exercised.<sup>11</sup>

Finally, the Canadian case *Re Bergethaler Waisenamt*<sup>12</sup> contains an extensive list of banking activities judicially noticed by the Manitoba Court of Appeal. It was thought that banking consists of receiving money on deposit from customers; paying a customer's cheques or drafts on it to the amount on deposit by such customers, and holding Dominion Government and Bank notes and coin for such purpose; paying interest by agreement on deposits; discounting commercial paper; dealing in exchange and in gold and silver coin and bullion; collecting notes and drafts deposited; arranging credits with banks in other towns, cities and countries; selling drafts or cheques on other banks and banking correspondents; issuing letters of credit; lending money on customer's notes, by way of overdraft and on bonds, shares and other securities.

A comparison of the three illustrations reveals that, although there are omissions and slight changes in emphasis in each definition according to the character of each country's banking system,<sup>13</sup> the

<sup>10</sup> Rule #1 of *Enemy Banking Business Rules* 1918 S.R.O., No. 1649, made under *Trading With The Enemy Amendment Act*, 1918.

<sup>11</sup> 9 *Corp. Jur. Sec.* 30 (s. 1). See also *Mercantile National Bank v. New York* 121 U.S. 138, 7 Sup. Ct. Rep. 826 for a similar definition.

<sup>12</sup> [1949] 1 D.L.R. 769 at 773.  
[1949] 1 W.W.R. 321 at 328.

<sup>13</sup> "Banking business in Canada . . . must be conducted on a broader and somewhat more elastic basis than in fully developed business communities such as Great Britain, and in construing the powers conferred upon banks to carry on 'such business generally as appertains to the business of banking' it is fair that Canadian conditions should be fully considered and allowed for" per Davies J., *Ont. Bank v. McAllister* (1910) 43 S.C.R. 338 at 353.

majority of the functions listed are identical. However, it is clear that none of the above definitions is exhaustive of banking as we know it today. For example, banks often act as executors or trustees and provide other services such as the safe-keeping of valuables.

The *Bergethaler* case provides an interesting example of how the first and second standards have been applied. The issue in that case was whether a provincial legislature could incorporate a loan, trust or financial company and vest it with functions which are carried on by federally chartered banks without thereby invading the exclusive legislative authority of the Dominion. Speaking for the Manitoba King's Bench,<sup>14</sup> Dysart J. applied the second test and found that a trust company which carried on many of the functions listed above was engaged in a banking business. The mere fact that the company did not repay its customers by cheque drawn on it but, instead, issued its own cheques drawn on a bank following an oral or written request from a customer, did not, in the light of the other banking functions carried on by the company, remove it from the federal jurisdiction. The Manitoba Court of Appeal, however, applied the first test and came to the opposite conclusion. It found that, besides the omission mentioned above, the company did not discount or lend on commercial paper but only on direct indebtedness, had no banking correspondents and did not make a practice of collection for customers or lending by overdraft. Thus, the company, in not fulfilling all the functions normally exercised by banks, was not engaged in "banking" as contemplated by section 91(15) of the B.N.A. Act.<sup>15</sup>

In the majority of the cases dealing with this subject, the courts, faced with the difficulties involved in formulating a comprehensive definition, have resorted to the third approach and attempted to discover the essential qualities of banking. Here, as in the first standard, the problem of historical development has arisen. For example, the use of the cheque in this century has become an integral part of modern banking. Lord Ashbourne C., in the Irish case of *In Re Shields' Estate*,<sup>16</sup> commented on this development.

The Bank of Ireland urge that the primal element in banking is the paying out money on cheques. This might be urged possibly now with some plausibility, but I do not think it could be so argued at the date of the passing of 33 George 2, c.14. The Bank of Ireland had not then been founded. Cheques were not at all as common then as now. Printed cheques were not then general.

Although the *Shields* case held that a person who took money on deposit account, paid interest thereon and made term and mortgage loans, was a banker even though he did not issue cheque books or honour drafts on demand, it is doubtful whether one could argue

<sup>14</sup> [1948] 1 D.L.R. 761, [1947] 1 W.W.R. 132.

<sup>15</sup> For an American decision holding that trust companies in Kansas were carrying on a banking business, see *State of Kansas ex. rel. Boynton v. Hayes* C.C.A. Kan. 62 F.2d. 597 where Pollock J. states at 601, "calling an institution a trust company does not prevent its being a bank within the meaning of the law, if it possesses and exercises all the powers of a bank."

<sup>16</sup> [1901] 1 I.R. 172 at 195.

nowadays that the cheque is not an essential part of banking business. As Paget says in his book on banking,

Some of the older dicta seem to give undue prominence to the deposit side of banking. In view of the provisions of the Bills of Exchange Act, and the later affirmation of cheque business as the leading feature of a bank, the scale would appear to have turned.<sup>17</sup>

The use of the cheque is but one of the developments which have given rise to two views on what comprises the basic qualities of banking. One view states that the fundamental features of banking are constant. It is only the modes by which the business is carried on that change. The other view asserts that banking may be defined only in terms of the methods by which it is performed. In support of the first view we find cases such as *State Savings Bank of Victoria v. Permewan, Wright & Co.*<sup>18</sup> where it is stated,

The essential characteristics of the business of banking . . . may be described as the collection of money by receiving deposits upon loan, repayable when and as expressly or impliedly agreed upon, and the utilization of the money so collected by lending it again in such sums as are required. . . .

The methods by which the functions are affected—as by current account, deposit account at call, fixed deposit account, orders, cheques, secured loans, discounting bills, note issue, letters of credit, telegraphic transfers, and any other modes that may be developed by the necessities of business—are merely accidental and auxiliary circumstances, any of which may or may not exist in any particular case.

Opposed to this static conception are opinions such as those of Lord Ashbourne and Paget quoted above which indicate that the key qualities of banking change as the business develops. In the American case of *Marvin v. Kentucky Title Trust Co.*, McCandless J., speaking for the Kentucky Court of Appeals, stated that

Originally banking seems to have been restricted to the receiving of deposits. With the development of the business came the discounting of paper, the loaning of money and the other varied activities in which modern banks engage. . . . Of course, in order to do a banking business, it is not essential for an institution to exercise all the powers permitted by its charter. But on the other hand, present day banking business is not to be confined to the narrow limits of its original inception. It is well known that insurance companies and other like institutions loan money, yet they are not banks. . . . Other illustrations might be given, but these are sufficient to show that the matter must be considered in a practical way and in the light of modern conditions. When so done, we think the above definition from *Warren v. Shook*<sup>19</sup> peculiarly apt: "Having a place of business where deposits are received and paid out on cheques, and where money is loaned upon security, is the substance of the business of a bank."<sup>20</sup>

It seems clear that this latter view is the more acceptable of the two. Certainly, it is the more practical approach to testing a business for the purpose of seeing whether it falls within a piece of banking legislation. The first view is wide enough to include many kinds of modern businesses which the courts would obviously not consider to be banking.

<sup>17</sup> *Paget's Law of Banking* (1961) 6th ed. 8.

<sup>18</sup> (1914) 19 C.L.R. 457 at 470.

<sup>19</sup> 91 U.S. 704.

<sup>20</sup> 50 A.L.R. 1337 at 1338.

What, then, are the basic qualities which the courts have held to be the essentials of banking? An early English case, which has been cited recently with approval, describes the principal part of a banker's business as receiving money on deposit, allowing the same to be drawn against as and when the depositor desires, and paying interest on the amounts standing on deposit.<sup>21</sup> A similar definition is contained in a 1932 Ceylonese statute which the Judicial Committee of the Privy Council thought accorded with the English law of that time. The statute defined a banking company as one which "carries on as its principal business the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheque, draft or order."<sup>22</sup> Paget has said that no one can be a banker who does not take current accounts, pay cheques drawn on himself and collect cheques for his customers.<sup>23</sup>

In the United States, it has been held that "a bank is an institution empowered to receive deposits of money, to make loans, to issue its promissory notes, or to perform any one or more of those functions."<sup>24</sup> The New York Surrogate Court has said that a commercial bank is one "making discounts, issuing notes and receiving deposits on which it may or may not pay interest."<sup>25</sup> These three basic functions are adopted in *Corpus Juris Secundus* as was noted above.

In an early Canadian case, *Proudfoot v. C.* examined the charters of various pre-confederation banks and stated,

The conclusion which seems to be deducible from these Acts is, that the business of banking consists in dealing in money, the precious metals, and in bonds and negotiable securities; that this dealing confers the power of lending on them or of purchasing them, whichever the bank directors may deem most for the advantage of the corporation.<sup>26</sup>

In the *Bergethaler* case, Coyne J. A. comments on the difficulty of defining banking, but perhaps overstates the problem when he says,

Banking is not a technical or legal term but a loose popular one, comprehending activities carried on by those who, likewise popularly, are called bankers. . . . Some are essential to the conception. But very few are exclusive activities of bankers. Chequing privileges accorded depositors, and general dealing in credit, are characteristic of and perhaps essential to banking. But even that does not make them exclusive rights of bankers. . . .<sup>27</sup>

Contrary to this view, it could be argued that such fundamental banking activities are exclusive to "banking", if not to "bankers", and the fact that other businesses carry on these activities does not make them any less essentially banking.

<sup>21</sup> *Re Bottomgate Industrial Co-operative Society* (1891), 65 L.T.R. 712, approved *R. v. Industrial Disputes Tribunal* [1954] 2 All E.R. 730.

<sup>22</sup> See: *Bank of Chettinad v. Com. of Income Tax* [1948] A.C. 378.

<sup>23</sup> Paget, *op. cit.* 8.

<sup>24</sup> *U.S. v. Papworth* 156 F. Suppl. 842 (adopting a definition from Black's Law Dictionary, 4th Ed.).

<sup>25</sup> *In re Wilkins Will* 226 N.Y.S. 415, 131 Misc. 188.

<sup>26</sup> *Jones v. Imperial Bank of Canada* (1876) 23 Gr. 262 at 275.

<sup>27</sup> [1949] 1 D.L.R. 769 at 778.

From the examples above, it would seem that the key qualities of banking are these. First, banking is primarily concerned with dealing in currency. Money is its commodity and its *raison d'être*. Secondly, the methods by which it deals with its commodity may be divided into primary and secondary. The primary methods are those which are most directly concerned with manipulating money as a commodity. Examples of these are the receiving of money on deposit, the paying out of money according to customer's cheques, the handling of foreign exchange, the lending of money on customer's notes, on bonds, shares and other securities and by way of overdraft. The primary activities are the basis of the third standard. They are the functions which comprise the very core of banking. The secondary methods are those which are not so basically concerned with the actual management of the bank's commodity, but some may involve the transfer of money in the ordinary commercial sense of buying and selling. Examples of these are the purchase of stocks and bonds, the safe-keeping of valuables and the giving of financial advice.

It has been argued that when a business carries on even one of the primary activities it may properly be called banking. In the *Bottomgate* case, Smith J. states,

Moreover, the business embarked on by the society when it took loans on deposit was in reality a banking business prohibited by statute. It is not necessary, in our judgement, in order to constitute a banking business prohibited by the statute, that the society should carry on every part of a business carried on by some bankers; it is sufficient to bring the business within the prohibition, if the society carried on what is the principal part of the business of a banker, *viz.*, receiving money on deposit, allowing the same to be drawn against as and when the depositor desires, and paying interest on the amounts standing on deposit.<sup>28</sup>

A similar trend of thought may be detected in the American cases. In *Reed v. People*, the court takes the following position.

Banks in a commercial sense are of three kinds—of deposit, of discount and of circulation. Strictly speaking, the term 'bank' implies a place for the deposit of money, as that is the most obvious purpose of such an institution. . . . Modern bankers frequently exercise any two or all three of those functions, but it is still true that an institution prohibited from exercising any more than one of the functions is a bank, in the strictest commercial sense.<sup>29</sup>

However, it should be noted that there is authority for the opposite view<sup>30</sup> and it is clear that the above opinion is open to the same objection as that raised against the view that the essentials of banking are traditional and constant. Both views allow a wide variety of businesses which are primarily not banking to come within the boundaries of the concept.

<sup>28</sup> (1891), 65 L.T.R. 712 at 714. See also Chorley's comment at page 24 of his *Law of Banking* 4th ed. where, after reciting Paget's essentials of banking (*supra*), he states, "It is not, however, easy to see why a banker should cease to be a banker (legally speaking—no doubt he would commercially) if he only accepted current accounts, or even if he refused to collect cheques."

<sup>29</sup> 18 N.E. 295, 125 Ill. 592; see also *State of Kansas v. Hayes*, 62 F.2d 597 at 600; *Fidelity Inv. Ass. v. Emmerson* 235 Ill. App. 518.

<sup>30</sup> *Dietrich v. Rothenberger* 75 S.W. 271 at 272; *Re Bergethaler Waisenamt*, [1949] 1 D.L.R. 769 at 776.

Apart from the three major approaches to the definition of banking which we have been examining, there is a further test which has been hinted at in the cases. The test itself has not been strongly asserted but one is aware, in reading the cases, that the thinking which underlies the test is an influence on the mind of the court. The test is whether the public considers the business in question to be banking. In *Re Shields' Estate*, Fitz Gibbon L.J. finds that the fact that Shields called himself a banker is of considerable importance.

In all his dealings with the public, Shields held his firm out as 'bankers'. He so described himself for the purpose of inducing custom and giving dignity to his operations. It may be conceded that people who are not bankers cannot make themselves so by adopting the name. . . . But the name was assumed by Shields and the Bank of Ireland accepted it as a truthful designation. . . . From beginning to end they treated him as a banker. That being so, it is only a question of fact, and one upon which the presumption is in the affirmative, whether there is reasonable evidence to warrant that Shields was what he professed to be, and what the Bank of Ireland took him to be, namely, a 'banker.'<sup>31</sup>

This 'holding out' test has been given weight by the courts because of the peculiar status of the banking business. The bank's role in society has always been of extreme importance. It stands at the centre of the economic community and enjoys a public confidence and trust. Such trust demands a high standard of conduct which has been assured in most countries by careful government supervision. This distinction between banking and other businesses is well illustrated by a comment from an American case which states,

Banks are quasi public corporations. They may only be organized in such manner and do such things as the state in which they carry on business permits them to do; and in carrying out its policy, the state has surrounded banking privileges with many wholesome restraints that are not applied to ordinary corporations. . . . The state, through its legislative department, has at all times exercised a careful and wholesome supervision over banking institutions for the purpose of protecting the general public from loss, while it has not, except in a general way, undertaken to control or interfere with the conduct of private corporations not invested with a public character or performing some public service.<sup>32</sup>

Thus, when banking is regarded in the light of "a public character or performing some public service" it assumes a stature which makes the use of the name 'bank', and the adoption of a banking facade of critical importance. In this regard, it is interesting to note that section 157 of Canada's Bank Act prohibits the use of the terms 'bank', 'banking' or 'banker' by any company except authorized banks.

In conclusion, there is no certainty as to which of the three major approaches the courts will use. Each standard merely represents a stage in a descending scale which is stringent at one end and flexible at the other. Probably, the approach most likely to be employed by the courts nowadays is one falling somewhere between the first and second standards. The expansion of business in general, which has produced encroachments on the traditional lines of demarcation between businesses, makes it necessary for the courts to

<sup>31</sup> [1901] 1 I.R.R. 172 at 197.

<sup>32</sup> *Bruner v. Citizens' Bank* 134 Ky 283, 120 S.W. 345.

apply an exacting test which is closer to the first or absolute standard than the other two. However, should the courts deem it advisable that corporations such as the loan and trust companies be brought under banking legislation for the protection of the public, it is conceivable that the third approach might be used.