Banksters, Bosses and Smart Money

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Almost a year to the day after the Security-Home Bank closed for good, the auctioneer began gaveling away a large collection of antique furniture, grandfather’s clocks, safes, and paintings. From the look of things, it appeared that the lavish “palaces of finance” that were the most visible symbol of the excesses that had brought the city of Toledo to ruin were being dismantled. Though much of the “lavish surroundings” of the “richly furnished” bank lobbies and executive offices were being inventoried and placed on the block, the truly important equipment was kept intact. Those attending the auction could not bid on adding machines, file cabinets, postal meters, and such sundry accounting equipment because they were still needed and would remain in use for over a decade to come.\(^1\)

It is commonly believed that when a bank closes, its activity ceases. In fact, a closed bank is a beehive of activity, and its closing merely marks a new phase in its business. Though a closed bank no longer accepts deposits, it still collects interest, deals in bonds, stocks, and real estate, and acts as a landlord, broker, and agent. In fact, the payroll of the banks under liquidation in Toledo actually increased when they closed, as there was much more “business” to be done than when they were open. Suddenly every outstanding loan had to be called in. Every last scrap of pledged collateral, which previously simply sat on the books, had to be revalued and much of it sold. Every skyscraper, warehouse, factory, bungalow, and lot mortgaged to the bank had to have its value assessed at the current market rate. Every stock, bond, and note had to be cashed in or sold. Within forty-eight hours of Toledo’s banks closing their doors, the state Banking Department had assigned sixty examiners and accountants on a three-shift rotation to augment the existing staffs of the banks in beginning these tasks.\(^2\)

A closed bank is not like any other business that, once closed, merely needs to sell off its inventory, machinery, and properties and repay its creditors with the proceeds. A bank is different from an ordinary business. A bank is merely
a collection of promises, not a physical thing. Its value consists of promises to hold and return deposits and promises to repay loans. Its property is merely tokens and records of those promises.

Before a bank has anything to actually “liquidate,” it must turn promises into things. But what happens when promises are broken? What happens to debtors who claim they haven’t the ability to make good on their promises? Someone needs to be in charge of negotiating and compromising all the thousands of claims for and against the bank. Here is the great complication and political nature of bank closings. He who controls the process of negotiating these promises controls how the money pie is cut up. If he is honest and neutral, he can act to maximize the pressure on debtors and recover the greatest sums possible to distribute back to the common depositor. But if he is self-interested, corrupt, or pursuing some other hidden agenda, he can use his power for his own ends and favor friends, punish enemies, cover up old misdeeds, and even rob the bank a second time. For those well-placed and alert to their opportunities, the closing of a bank was a tremendous windfall.

The first legal skirmish fought in the wake of the banks’ collapse was over just this question of who should be in charge of the process of liquidation. One enraged depositor filed suit in local court to place the Security-Home bank in the hands of a court-appointed receiver so as to safeguard its assets in the interest of all general depositors. Though the suit named the directors of the bank as defendants, it was the superintendent of banks and Ohio’s attorney general’s office who fought the action. Joining the State of Ohio alongside the names of the directors of the bank in their rejoinder, the assistant attorney general on the scene in Toledo proclaimed that he would “resist to the last ditch any effort at private receivership.” Backing up his promise, the attorney general’s office brought out its big guns, enlisting Brown and Sanger, the law firm of Republican bigwig Walter Folger Brown, to assist it in the case.\(^3\)

In heading off the movement to appoint a private receiver, the attorney general’s office was interested primarily in keeping control of the bank liquidation process within the confines of the Department of Banks. Were the process to take the route of a normal bankruptcy, all the essential investigations and decisions would be in the hands of a local judge and all the receiver’s actions would be placed in the public record. Both the attorney general’s office and the superintendent of banks wanted to be sure that they would have control over not only the disposition of the bank’s assets, but also the auditing and gathering of information about the circumstances of the collapse itself. Since, as their subsequent actions would reveal, the state used its control of the process to prevent the release of embarrassing details to
the public, preventing the appointment of an independent receiver was essentially the first step of what would become a long cover-up.\textsuperscript{4}

In very short order the court ruled in the state’s favor and allowed the Department of Banks to run the liquidation. Toledo’s civil court, though ostensibly the watchdog of the liquidation process, seldom second-guessed the actions of local bank liquidators and rarely questioned the decisions of state bank officials. According to state law, it was the court’s responsibility to approve each sale of securities or properties and to give the public at least ten days’ notice before passing on the issue so as to guarantee that the interests of all the depositors were being protected. But soon after dismissing the motion demanding a private receiver, a county judge granted blanket permission to the deputy superintendents in charge of liquidation to sell securities and properties when and how they deemed most advantageous to the bank.\textsuperscript{5}

From that point most of the liquidators’ decisions were not recorded or reported as the law required. The selling of tens of millions of dollars of assets, the compromising of millions of dollars of loans, and the disposition of tens of thousands of depositors’ savings took place in secrecy. Though this policy may have given the liquidators the flexibility to sell properties when the market was advantageous, it also introduced the possibility of sweetheart deals for insiders made well out of the public’s view.

Ohio’s Banking Department assigned its own employees to head the liquidation of Toledo’s banks, a move which lent the appearance of neutral government supervision to the process, but actually employed the banks’ existing officers and staff to run things. Though these official “deputy superintendents” in charge of liquidation were outside professionals with no vested interests in the banks they were appointed to supervise, they had no hand in the day-to-day operations of their banks. Deputy Superintendent in charge of the Security-Home Bank, J. C. Van Pelt, later recounted that when he was called in to oversee the bank he relied entirely on the existing Security-Home staff because “there was considerable confusion in the Department by reason of that closing and due to the lack of experienced persons.” The scale of the bank, the height of the mountain of paper to be turned into cash, the seemingly endless extent of files to be opened and reassessed made it “physically impossible,” Van Pelt explained, for him to actually examine or review any of the assets himself. So rather than actually get dirty in the paper himself, Van Pelt issued guidelines and policies and allowed the bank’s own officers to assess and negotiate its properties. “I merely prescribed the form,” Van Pelt confessed, “and directed others in the preparation.” As a result, some of the most egregious frauds evident in the bank’s accounts were easily buried by the very bank officers who had profited by them. It was
seven years later before the first of hundreds of forged mortgages surfaced out of the muck.⁶

Even higher officials of the failed banks kept their posts and now drew their checks from Columbus as assistant liquidators. James W. Eckenrode, the longtime assistant treasurer at the Ohio Bank, was kept on as an assistant liquidator. Karl Rumpf, the assistant secretary of the Security-Home bank and former vice-president of the Dime Bank, kept his position running the mortgage loan department. This was a key position, as Rumpf had the power to negotiate compromises and offsets with those owing the bank money. One former bank official later testified under oath that Rumpf was quite accommodating to this fellow insider, forgiving much of his indebtedness.⁷

The most sensitive areas of the banks, their trust departments, remained in the hands of the same bank officers who had run them for years. According to another deputy superintendent, William M. Konzen, “in my experience in every instance [the] men [put] in charge have had previous trust experience and were in the various trust departments prior to the closing of the bank.”⁸ These were the most significant departments to have such a continuity of management because it was in the trust departments where evidence of the most clear-cut fraud and malfeasance was to be found.⁹ These departments moved money-losing subdivisions off their books and shifted them into real estate trusts. These trusts would either “purchase” the bad paper from the bank, or, more commonly, they would pool the trash properties into one shell corporation that would issue shares back to the bank. The shares could then be carried at full value on the bank’s ledger while the trust hid the true losses the bank had incurred. Konzen later noted that “Toledo banks I think are particularly noted for carrying real estate and various assets in trust securing commercial obligations,” and estimated that between 500 and 1000 such agreements existed in all the failed banks whose total face value ran up to eight million dollars.¹⁰ Trusts were also the place where fictional government bond accounts were set up for the convenience of insiders and high rollers to hide their money from the tax man. When the state allowed bankers to keep active managerial control over their trust departments, it effectively granted them the ability to conceal their most dangerous secrets.

Control of the banks’ trust departments was also prized because trust funds were deemed privileged deposits by Ohio’s courts. While general deposits would be paid back a small fraction at a time as loans and properties were sold, trust accounts were liquidated and returned individually. For those wealthy folks fortunate enough to have exclusively cash in their trust accounts, their deposits would be returned in full. Other individuals whose trust accounts held mainly securities would receive their notes and certificates back. Only
in cases where the trust was owned in shares by investors would the trust’s assets be sold or compromised for cash.

The privileged status of trust accounts provided yet another backdoor means for the well-connected to recover a higher proportion of their deposits than the average person. As soon as the banks closed, several trust department managers began shifting cash that was held in commercial accounts to their trust accounts. In less than three weeks after it closed, insiders at the Commerce Guardian Bank had transferred $317,595.75 from the general pool of deposits to trust accounts, to cite just one example from one bank that came to light.\(^\text{11}\) Every dollar moved in this way cut into the sum that regular depositors would someday recover.

Next to bank managers themselves, the other critical area of staffing for the liquidation department was in the field of assessments. Before the banks could begin to negotiate the repayment of loans or the selling of batches of mortgages, the true value of these properties had to be determined. The banks’ own estimates of their value were useless, as banks had routinely inflated values so as to balance their books or to maximize the leverage of the collateral of favored debtors. No one could ignore the fact that vacant lots which could not fetch $40 in 1929 were listed on the books of the Security-Home Bank for $1,500. Worthless bonds were carried at their face and the worth of shares in real estate trusts were anybody’s guess.

Here again, the need for independent and unbiased appraisals was paramount, and the danger of self-interested distortions of actual values was high. Many businessmen owing loans to the bank hoped for a high assessment on their collateral so as to walk away clear or even earn a profit when the loan was cancelled. In the most direct way, overvalued assessments ate away at the body of cash to someday be returned to the thousands of ordinary depositors. Though the task of selecting neutral assessors may have been one of the most important tasks in the hands of the county courts, a party functionary like Judge Charles M. Milroy probably viewed the opportunity to hand-select seventy-five men for decently paying jobs in the midst of mass unemployment as a partisan bonus. Besides the usual political flunkies who now owed the party a favor come election time, Milroy selected a surprising number of Toledo bankers to assess Toledo bank assets. The first group of seventy-five assessors were charged with assessing the mortgage portfolio of the Ohio Bank. Eight of those selected were present or past bank directors, including Carl Mehring, a director of the Commercial Bank, Charles L. Medaris, director of the Commerce Guardian Bank, and John Huebner, who not only sat on the board of directors of the Security-Home Bank, but owed it $11,475 when it closed.\(^\text{12}\) Judge Milroy then picked Claude Campbell to lead the seventy-five men in their work. Campbell was then a vice-president of the Ohio Bank.\(^\text{13}\)
For the more potentially scandalous task of assessing the value of commercial and personal loans in the Ohio Bank, a committee of five assessors was selected by Judge Milroy. Three members of this committee were each directors of the other large busted banks, and a fourth was the assistant secretary of the Security-Home Bank. Likewise, eight of the nine appraisers appointed to do the same job for the Security-Home Bank were bank directors, including one, W. C. Carr, who was its sitting director! Just in case one of these nine men could not complete the work, the judge appointed Albert V. Foster, a vice-president of the Security-Home Bank, as an alternate. Whereas the lowly mortgage assessors earned a piece rate of $3.00 per assessment, those serving on these special committees were reported to have been given a flat salary of $1,000, paid for out of bank assets.\(^\text{14}\)

Almost immediately after the assessors began, complaints were made of the slipshod way they did their work. The \textit{Blade} reported the manner in which some of the appraisers went about their work:

\begin{quote}
“What is the size of this lot, about 30 by 40?” [asked an appraiser]
“No, it is about 50 feet by 60 feet,” the appraisers would be told.
“What do you think the place is worth, about $3,000?” the appraisers would ask.
“Yes, I would think it would be worth about $3,000,” the tenant would say.\(^\text{15}\)
\end{quote}

More than a few of the appraisers seem to have followed this sort of routine. Those who were paid by the assessment had an interest in finishing them as quickly as possible. Others had obvious potential conflicts of interest. No complete published figures of these assessments exist, though an indication of how they ended up can be glimpsed in one fragmentary document that was later publicly released. Two years after the assessors completed their work, their estimation of the value of the properties that the banks owned outright was published. This estimation did not include any of the properties or securities held as collateral, only properties held free and clear. Before they closed, the banks appraised their own real estate as being worth $13,438,363.94, a sum acknowledged to have been wildly inflated, while the court-appointed appraisers, after months of work, estimated their worth at $13,177,632.94. In the end, the court’s assessments of bank-owned real estate varied from the bank’s own stated values by less than 2 percent, a ludicrously small margin.\(^\text{16}\)

The greatest power that bank liquidators wielded was the authority to grant offsets. An offset is a bargain whereby a person who owed a sum of money to the bank while also holding a deposit in the bank exchanges the
one for the other. The deposit is offset by the loan and both deposit account and loan are cleared off the books. In theory this is a very rapid and low-cost means of liquidating bank assets, as there are no brokerage or lawyers fees or other costs associated in collecting on the loan. But in practice, offsets provide a means whereby some privileged depositors are able to reclaim their frozen deposits at the expense of all other depositors. This occurs because those depositors not owing loans to the bank will ultimately reclaim only a fraction of their money, and that only over many years of small dividends, while those with substantial loans are able to reclaim a larger percentage of their deposits immediately.

While the banks were in the process of collapsing, and while they were still under private control, anticipated offsets were employed by bank insiders, the so-called “smart money,” as a devious means of closing out their deposit accounts. After they failed, even though their titular control passed to the state, because the state Banking Department retained the banks’ old staff and officers to serve as their liquidators, offsets continued to be a means whereby the “smart money” could rescue their cash, and, in some cases, even take advantage of the bank’s failure and turn a tidy profit.

Of all the aspects of the bank failures in Toledo, the least well documented is the scope and nature of the offsets that were granted to some depositors. The local courts did not require liquidators to file a complete report of these compromises that would have entered the public record, as required by state law. After the Toledo liquidations were declared to be complete, all the detailed records of these transactions were sent to the incinerator. All that the historical record contains are the total figures for each bank. But even in the aggregate, it is clear that the power of granting offsets was abused.

Immediately after the banks were closed and handed over to the state for liquidation, the market value of deposits lost over two-thirds of their value. The savvy and impartial liquidator would therefore never think of granting offsets on an equal dollar-for-dollar basis between loans and deposits. Instead, he should take a larger share of loans to deposits proportionate to the shrunken worth of the average depositor’s bank book. Debtors who don’t like the deal are free to repay their loans as previously contracted, but most, in the Depression environment of tight money, would likely take the deal rather than incur more debt or sell other assets at a loss to make good on the loan. Therefore, the leveraged power of offsets should show up in the bank’s liquidation reports as each dollar of offsets retires a greater percentage of outstanding loans than do dollars taken in payment. For the Toledo banks, where frozen deposits were generally accepted as being worth about 30–35 cents on the dollar, when the total cash income of the liquidated bank is subtracted from the total of cancelled loans, the remainder should exceed
offsets by a significant factor. By the time of the first accounting of the progress of the liquidation of Toledo’s four largest banks, offsetting deposits leveraged an average of just 6 percent additional loans. More puzzling, the bank whose deposits had arguably fallen to the lowest value, Security-Home Bank, managed the lowest leverage percentage of offsets in the city—just 4 percent additional value.

A very few instances of the practice of offsetting made it into the press. In November of 1931, the Stollberg Hardware and Paint Company swapped a deposit of $10,633.11 for $10,232.48 that it owed to the bank, a margin in the bank’s favor of just 3.8 percent. More suspiciously, the liquidators of the Commerce Guardian Bank cancelled a $200,000 loan to the Detroit and Toledo Shore Line Railroad in exchange for a $500 savings account. This may have had something to do with the fact that Walter Lint Ross served as both vice-president of the Commerce Guardian bank and a director of the Detroit and Toledo Shore Line Railroad.

In the case of only one bank are even aggregate numbers of offsets available. During an Ohio Senate investigation in November of 1934, the state’s investigator reported that the Ohio Bank had made $1,332,272.09 by offsetting deposits. By the end of 1934, the Ohio Bank had offset a total of $10,886,034 worth of its deposits. Comparing these numbers indicates that on average, the bank allowed 89.1 percent of the worth of deposits in offsets.

The scale of Toledo’s offsets dwarfed anything seen in the state before. In just six months, $9,815,425 worth of deposits were offset in exchange for an unknown sum of credits. This amounted to 61 percent of all the offsets allowed among the twenty-seven largest bank failures in the state in that year. The volume of offsets granted by both the Ohio Bank and the Security-Home Bank were double the total of any other institution in Ohio.

As the bank liquidations dragged on into the winter months of 1931–1932, the mechanism of offsets became a great potential source of profit for the banks’ wealthiest debtors. One of the first public actions taken by the Department of Banks was to issue a certificate of claim to every depositor who brought his or her bank book into a bank to be verified. Though they were probably not meant to be so, these certificates were fungible, allowing for the sudden creation of a new and lucrative market in the buying and selling of bank deposits. Offering dimes on dollars, brokers would purchase the certificates of destitute depositors who were desperate to get whatever cash they could immediately. They would then turn around and sell them to those owing large loans to the banks. Those purchasing the certificates would then present them as offsets for their debts to the bank and free themselves from their obligations for a fraction of the face value of the loan. In this way the very bankers who had given themselves large last-minute loans
and thereby hastened the bankruptcy of Toledo’s banks found yet another way to profit from the financial destruction they had helped create.\textsuperscript{23}

A burgeoning market for depositors’ claim certificates provided a ready means for those with both money and debts to actually turn a profit from the bank failures. For example, one unnamed county official owed one of the banks $27,000 on a real estate investment. He purchased $45,000 in other depositors’ claims for thirty cents on the dollar, costing him a total of $14,000. After he swapped these certificates with the bank wiping out his debt, he cleared $13,000, or a 48-percent profit.\textsuperscript{24}

Banks accepted claim certificates in lieu of cash when selling off their assets as well. This allowed investors to gain twice by the liquidation—once by purchasing property at fire-sale prices and a second time by paying for them with discounted deposit certificates. Again, no records of these deals were kept by the banks or the local courts, but one newspaper did detail one such bargain that occurred in January of 1933. The Ohio Bank sold $20,000 in Allen County, Ohio, bonds to an unnamed investor for $23,188 in deposit certificates. At the time, the bonds sold for cash for about $9,600 and the certificates for about $7,000, netting either an immediate $2,600 profit or the potential for the bonds’ ultimate redemption at face value sometime in the future.\textsuperscript{25} David A. Yoder, the president of a large dairy company, arranged an offset that “caused much comment about town.” Yoder happily exchanged $266,000 worth of claims that he had purchased from brokers at the going rate of around 35 cents on the dollar, swapping them at full face value to cancel out a loan of $266,000 he owed the Ohio Bank. The Ohio Bank was known to grant up to 100 percent credit to corporations it was itself heavily invested in, yet credited the city of Toledo only 38 percent in offsetting its loans and deposits.\textsuperscript{26}

Sixteen loan companies and brokers competed to purchase depositors’ claim certificates by the end of 1931. The field was fertile enough to encourage a half-dozen additional companies to enter the business over the next year. Among the claims brokers who engaged in this business were a number of Toledo’s prominent bankers. Kenton D. Keilholtz, a director of the Security-Home Bank up to the day it went bust, was also first vice-president of the Financial Securities Corporation, a no-collateral personal loan operation. Pratt Tracy, who directed the Ohio Bank to ruin, was vice-president of the Toledo Citizens System Company, which offered “character loans to wage earners.” Tracy’s partners in this venture were Robert J. West, a director of the Security-Home Bank, and Harry W. Wachter, director of the Commercial Bank. Interestingly, Toledo Citizens System Company’s president was none other than Mayor William T. Jackson, the political figurehead of Toledo’s financial titans.\textsuperscript{27}
The most prominent and aggressive of the newcomers to the claim certificate business was organized near the one-year anniversary of Toledo's bank crisis by a number of former bank executives. Named the Toledo Guaranty Corporation, it was run out of the old east side branch of the Ohio Bank by O. D. Tiffany, former president of Peoples' Savings Bank, U. G. Denman, former director of the Commercial Bank and former attorney general of Ohio, and W. R. Parmele. Unlike the other bank deposit brokers who swapped claims for cash, Toledo Guaranty looked for greater profits by offering depositors shares of the company's own stock or their own bonds that sported an irresistibly high interest rate on their face.

Most of the money Guaranty received from its first sale of deposits went into an extensive advertising campaign aimed at convincing those still holding onto their claims to deed them over the company: “WE CAN PUT YOUR CLOSED BANK ACCOUNT TO WORK!,” screamed one full page ad, “. . . [we] have a unique, financially sound plan for putting closed bank accounts to work.”

Though he was president of the firm, O. D. Tiffany began to smell a rat when his manager, Parmele, refused to let him examine the books. Tiffany quickly resigned, suspecting correctly that the company was little more than a pyramid scheme.

The large scale of the market in bank deposit certificates was not made clear until years later. The state Department of Banks did not report figures for the amount of savings bought and sold in this way until 1935. By then $13,672,087 worth of deposits had been sold to the four principal banks being liquidated. This sum was equal to roughly 25 percent of the total amount of deposits written off their books by that time. Statewide, only about 5 percent of deposits were retired in this way.

By March of 1933 the proliferation of storefront brokers specializing in deposit certificates reached the point where the attorney's general office felt compelled to step in and warn all dealers that only those firms holding a license to trade in securities were legal. Toledo's Better Business Association formed a special committee to investigate the industry. Both the actions on the part of the state and those of local businessmen were aimed not at restricting the market in deposits but merely at eliminating the smaller fly-by-night brokers. The Better Business Association's committee included real estate developer Zale Reuben, whose Reuben Securities Company was a prominent dealer in deposits, and W. C. Carr, a banker who went directly from piloting the Security Home Bank onto the rocks to profiting from the trade in bank deposits with the B. K. Blanchet Co.

Unfortunately, the Better Business Association proved a poor watchdog. During its tenure an apparently reputable firm, the Louis B. Storer Co.,
enticed Ada E. Wilson, a retired elementary school teacher, to swap her $2,200 in Security-Home Bank claims for some other stocks. Soon after taking her claims, Storer closed up his shop, and Mrs. Wilson never heard from him again until he stood before a county jury and was declared guilty of fraud.\textsuperscript{32}

Judge James S. Martin, who was at that time one of the jurists supervising the liquidation of the banks, condemned the entire deposit certificate business, criticizing “those who prey upon depositors forced to sell accounts for the necessities of life,” but he also understood that little could be done legally to curtail it. Instead, Martin suggested that the state Banking Department provide the public with a frank estimate of the likely pay-out of each bank and a calculation of the fair cash value of deposits at the current time. Such a step would help ensure that those selling their claims would not be exploited by businessmen willing to exploit their desperation. But, Martin concluded that the state Banking Department would never provide the public with the real figures because it would be just too embarrassing.\textsuperscript{33}

Apparently Judge Martin’s suspicions about the Department of Banking were correct. Throughout the process of liquidation the Banking Department jiggered the numbers released publicly so as to make it appear that the banks were repaying a greater proportion of their deposits than they actually were. It was not until 1935 that the department revealed the sum of deposit certificates that had been sold to the banks, though the practice had gone on since the early days of the liquidation in 1931. Before 1935, the department did not report the total shrinkage or loss of resources as a result of liquidation, an important indicator of the likely returns to depositors. Most significantly, the Department of Banking reported a total figure for the percentage of deposits returned to depositors that did not reflect the fact that different classes of depositors received different rates of return.

For example, in 1935 the department boasted that it had returned over 70 percent of its $38,880,329 in deposits to the depositors of the Ohio Bank. In calculating this sum, the department lumped together the value of offsets, preferred claims, the deposits of other banks, deposit certificates surrendered, and public funds. Some time after the Ohio Bank closed, all the money that was deposited as a reserve from other banks, $1,504,445, was returned in full. All the money that was deposited on behalf of trust funds, $2,087,324, was also fully repaid. Then there was another $2,004,078 of public funds on deposit, mostly taxes, that was, after some litigation, counted as a preferred deposit and returned to various town, county, and city governments. A total of some $3,832,233 worth of deposits were off-
set by loans, and a whopping $7,053,801 worth of deposits were sold to the bank by people other than those who originally held them. That left less than a 50 percent dividend for the common depositor.

What all these numbers add up to was a class system at work in the liquidation. Roughly (and these calculations must be rough, given the destruction of more detailed bank records), 10 percent of deposits, claimed as protected trust funds but never actually invested in securities, were returned at nearly their full value. Another 10 percent was offset for loans at a rate more advantageous than that found in the open market for deposit certificates and in many cases close to par. About 20 percent of deposits were sacrificed to brokers at a severe discount. The remaining 60 percent of deposits realized below 50 percent of their value. Rates in each category differed for each bank, though each had the same stratification of classes who benefited unequally in the liquidation.14

While insiders clearly had an advantage in the course of liquidation and were able to liberate a higher percentage of their deposits from the closed banks than the average person, they also bore one unique legal burden that was not easily shaken. Every shareholder in a bank was obligated to pay an amount equal to his or her investment into the bank when it failed. This provision, commonly known as “double liability,” was the most firmly established banking law in Ohio, having been written into the state’s constitution of 1851. For many decades the double liability provision served as the only legal safeguard for the good conduct of bankers.35 When Ohio legislated more specific regulations for corporations and banks, the constitutional provision of 1851 remained primary and could not be modified or limited without constitutional amendment. The double liability law was reaffirmed immediately after the Toledo bank crash by the Supreme Court of Ohio, which ordered that those owing banks a double liability payment could not have them set-off equally by their own deposits “except so far as dividends may be paid thereon.”36 In other words, there was no quick or privileged way for bankers to shed their liability, so they simply didn’t pay them.

Three years after the collapse, only slightly more than half of bank shareholders who had been ordered to pay their liability had done so. Some, like a group of investors owing nearly a half million dollars to three of the closed banks, legally delayed payment for two years by contesting the right of the superintendent of banks to be the state’s collector.37 Others simply ignored their bills. Interestingly, the shareholders who had ponied up the most cash, about 10 percent more than the average, were those whose bank was under the most legal attack, the Security-Home. The Ohio Bank’s shareholders were the most delinquent, probably because they had watered their stock more than most in the years before the crisis.
A peek underneath the totals reveals a predictable trend: the most responsible shareholders owned the fewest number of shares. The numbers are only available for the Commercial Bank, the smallest of the four big failures, but there is no reason to believe these trends were not true at the other banks as well. Only 39 percent of shareholders whose shareholdings amounted to more than $1,000 had paid their debts, while exactly half of those whose shares totaled less than $1,000 had done so. The three investors who were the principal owners of the bank, who held nearly a third of all shares in the bank, or a total of $205,300, or more than three times the holdings of all investors owning less than $1,000, had together paid off only 10 percent, or $21,178.24, of their liability.

Though the state Banking Department eventually won judgments against the largest recalcitrant shareholders, the complexity of their financial and business dealings provided many places for them to hide their money and stave off payment. F. E. Stewart, former vice-president of the Commercial Bank, had succeeded in paying only $45.55 of his $64,150 stock liability by the time he was dragged into Judge John McCabe’s court in January of 1934. Stewart was quizzed by a private attorney, Nolan Boggs, hired to recover as much money as he could by the state on a commission basis. Though he didn’t admit this to the judge, Boggs himself had once been a shareholder of the Commercial Bank; however, unlike Stewart, he had paid his own liability of $800 in full. Boggs was after several hundred shares of Kennecott Copper and Packard Motors that Stewart had squirreled away in a safe deposit box. Being a sharp banker, Stewart knew that trust funds were protected from being seized and claimed that he had privately pledged the stock to the support of his ninety-year-old, blind mother. Boggs then went after $2,800 in cash that Stewart then claimed was actually an inheritance given to his wife. Finally, Boggs zeroed in on a stash of government bonds, worth in the neighborhood of $7,880. Stewart claimed that these belonged to his wife and that she had loaned them to him in exchange for 50 shares of Commercial Bank stock as collateral. The idea that Stewart needed to secure a loan from his wife with collateral, if true, might have revealed a certain shakiness to their marriage. What is more strange is that Stewart did so just a few weeks before the Commercial closed, a tacit admission that he had swindled his wife. In the end Stewart’s testimony didn’t convince the judge, and most of the securities were awarded to the liquidators and Boggs made a fat fee which was also paid out of the Commercial Bank’s assets, scratching a little bit more from the withering pile left to divide up among the depositors.  

Besides simply not paying, there was only one way for a shareholder to avoid paying the face value of their shares back to a failed bank. If the bank
could be reopened or reorganized, double liability might be waived by the superintendent of banks. For this reason, even banks that had been thoroughly looted by their owners attempted to reopen. However, like every other question involved in bank liquidation, the decision of which banks would reopen and which would be dissolved lay not in the public realm, but was decided behind the scenes among a very small group of players. This select group of men did not base their decisions on considerations of public necessity or convenience but made the process a continuation of the competitive struggles for financial control of the city that had existed before the banks closed.

The only way a bank in as much trouble as Toledo’s closed banks could possibly reopen was to secure some sort of outside loan guarantees and a quick infusion of cash. Only one of Toledo’s four big closed banks, the Commerce Guardian bank, received such aid. It was the only one of the four that was a member of the Federal Reserve System, giving it easier access to federal loans than any other. The others looked to the Reconstruction Finance Corporation for help.

The RFC had been created late in Hoover’s administration to provide loan guarantees to corporations and banks that were on the verge of sinking beneath the Depression’s waves. Congress allocated $500 million of seed money to establish the RFC’s loan fund and gave the quasi-public corporation permission to issue its own bonds worth up to three times that. Unwilling to make it a permanent wing of government, Congress also placed a one-year sunset provision into the bill, ensuring its demise after one year unless renewed by order of the president. From the start, President Hoover, who was uncomfortable with the very concept of the RFC, organized its structure so as to decentralize its functions out of Washington. Rather than having Washington bureaucrats reviewing applications for loans, the initial screening process devolved to thirty-three local agencies peppered throughout the nation. These review committees were staffed not by disinterested government professionals, but by local bankers. Such an organizational tree certainly avoided Hoover’s fears of creating a mushrooming bureaucracy that would lord over private citizens from a distant capital city, but they allowed local rivalries, jealousies, and competitive pressures to enter the process of loan approval from the very start.

Such parochial considerations came into play when a group of activists attempted to secure federal aid to reopen the Ohio Bank. Composed of a number of small shareholders in the Ohio Bank along with a few others who had no direct financial stake themselves, the Ohio Bank Depositors Committee was initially optimistic that federal loans would be steered their
way. They had good cause: their local party boss, Walter Folger Brown, was a member of Hoover’s cabinet and one of the president’s most trusted political advisors; a local man, W. W. Knight, was a member of the Federal Reserve Board for the region; Henry Thompson, president of the Toledo Trust bank, was a member of the RFC loan committee for the Cleveland district that included Toledo; and, finally, when President Hoover visited Toledo in September of 1931, he promised aid for the city. In less than a year of effort, the Ohio Bank committee had received a warm endorsement of their plan for reorganization from Governor George White and had begun collecting the thousands of consent forms from depositors pledging their deposits to the new venture.

In spite of, or perhaps because of, Toledo’s political muscle in the state and even the nation, the Ohio Bank reorganization plan began encountering unexplained obstacles. Just before Christmas of 1932, one depositor, Eugene Rheinfrank, sued the state Department of Banking, asking a judge to order it to distribute an immediate dividend to the Ohio Bank’s creditors. Superintendent of Banks Fulton then indicated his support for plans to reorganize the bank rather than to pay out more of its cash immediately, writing to the reorganization committee that were a dividend issued, there would be no chance of the bank ever reopening. But just three days later, Fulton reversed himself, saying that the existing plan was insufficient and that more cash would have to be infused into the bank before it could be restarted.

The historical record is disputed as to what happened in those three days to change Superintendent Fulton’s mind. All sides admit that during one of those days, Fulton had a meeting with three important Toledo industrialists, Frank Collins, W. E. Levis, and E. J. Marshall, at the Deshler Hotel in Columbus. This meeting aroused suspicions among those pushing for the Ohio Bank’s reopening because Collins and Levis were in charge of the reorganization of the Commerce Guardian Bank and Marshall was one of its former directors. The leader of the Ohio Bank’s reorganization effort claimed that Collins returned to Toledo and openly boasted that the Ohio would never reopen. Fulton denied to an Ohio Senate investigating committee that he had discussed the Ohio Bank issue at the Deshler meeting, though his attorney later “revised” his statement for the record, admitting that Fulton had been informed that Collins and Levis opposed the Ohio Bank’s reopening, but not by them directly (leaving open the question of whether Marshall lobbied against it on their behalf). Walter Baertschi, leader of the Ohio Bank depositors association that was spearheading the Ohio’s reorganization drive, later charged that Collins and Levis had even threatened him. Though there is not enough evidence to prove that the
Commerce Guardian faction was pulling strings to block the Ohio Bank’s reopening, it is certain that these men would have had an interest in limiting the growth of competition to their fledgling bank.

Beyond the charges flung at the Commerce Guardian group, there was other evidence that someone was actively working to keep the Ohio Bank closed. Testifying before the Ohio Senate Banking Committee, Superintendent Fulton described how the Reconstruction Finance Corporation in Washington stonewalled his efforts to aid the Ohio Bank’s opening. In spite of his lobbying, Fulton said, the RFC would only agree to give a loan to help liquidate the bank, not one to help it open. Fulton’s attorney added that the depositors committee’s complaint was “with the RFC. They evidently told [them] one thing and the department [of banks] another.”

If there was a cabal of Toledo financiers working to block the reopening of the Ohio Bank, what could have been their motive? Walter Baertschi had one theory: “We have felt right along that we could not open because the opening would be a loss by withdrawal of four million dollars of Ohio funds to the Toledo Trust Co. and the withdrawal of other monies by loyal depositors of the Ohio who would rush to return to that bank.”

One outspoken editor of a small-circulation weekly newspaper also saw the evidence as pointing to a Toledo Trust conspiracy:

The facts are these: Walter F. Brown, former Postmaster general, is a member of the Federal Reserve Board of this district; he is also director of the Toledo Trust Co. W. W. Knight, vice-president of a big hardware company, is a member of the Federal Reserve Board; he is also a director of the Toledo Trust Co. Henry L. Thompson, president of a big hardware concern, is also president of the Toledo Trust Co. and a member of the R.F.C. in Cleveland.

You get the point? All three of them are naturally interested in the welfare of the Toledo Trust Co. . . . These three men, with their financial associates, undoubtedly have great power and influence with the recommendations of the R.F.C.

There is no doubt that Toledo Trust viewed the collapse of the other banks as its one great chance to gain unrivaled supremacy in what had long been a hotly competitive financial market. On August 20, 1931, less than a week after the bank closings, Superintendent Fulton ordered that all the cash and securities in all the shuttered banks be transferred to the Toledo Trust Bank, immediately increasing Toledo Trust’s deposits by millions of dollars. The
very next day, Toledo Trust opened its first branch bank, in an old location of its nemesis, the Security-Home Bank, on Starr Avenue. The following day it opened the second branch bank in its history, at another Security-Home building on the busy commercial intersection of Monroe and Detroit. By the end of the week, Henry Thompson gleefully reported that his bank’s deposits were up four million since the bank crisis began. By the end of the year, with all the added business, increased deposits, and expanded branches, Toledo Trust was forced to expand its payroll from 118 employees to 201.

Interestingly, the first RFC loan to reach Toledo benefited a handful of directors of Toledo Trust. In early 1934, a $700,000 loan was approved to assist in the reorganization of the First National Bank, a small federal bank that capsized in the fall of 1931. As part of its reopening, the board room of First National was emptied out and a new slate of directors was put in place. Both vice-presidents, Rathbun Fuller and George R. Ford, were directors of Toledo Trust. Additionally, Fuller also served as Toledo Trust’s corporate attorney. One other longtime director of Toledo Trust, Gordon Mather, took a chair with the First National’s board. On the surface of things, this RFC loan seemed not only to assist in the reopening of a rival bank, but to engineer its quiet takeover by Toledo Trust interests.

There can be no doubt that Henry Thompson and the other men deeply invested in the Toledo Trust were well positioned politically to have blocked federal loans to the Ohio Bank. Whether he or his associates did so in fact will for now have to remain an unanswered question. Thompson’s group were not the only powerful players who might have worked to block the reopening of Toledo’s other closed banks. Backers of the Commerce Guardian reopening, men who stood to lose their exemption from payment of their double liability if their project failed, were also alleged to have meddled in the process. If either of these well-connected and influential financial factions had intervened in the Ohio’s bid to reopen, their political weight would have easily crushed that of the Ohio’s reorganization committee, which was composed of men of modest means who had no chits to be called in with political parties and whose anger exerted no fear among policymakers. The few men associated with the Ohio Bank who could call in favors, who could command consideration of their wishes, and whose wrath carried consequences for anyone seeking office or appointment, such as the Ohio’s president George Jones and his business partner, Willard Webb, reportedly had no interest in the bank’s reopening once they had paid their liability assessments. Eventually they found it easier to simply buy a stake in a new bank, Citizens Savings, that was organized in the spring of 1932. In the end the Ohio Bank remained closed and was not finally liquidated completely until 1943.
On average, the liquidation of Toledo’s closed banks stretched over more than a decade, and when it concluded it remained unclear just how much the average depositor was repaid. The liquidation of Security-Home Bank was officially declared complete two weeks after the bombing of Pearl Harbor. The state Banking Department triumphantly reported that nearly three-quarters of all the deposits in the bank had been repaid (73.5 percent). This number, however, seems to have been purposely inflated. One indication of this is that the total amount of deposits used as the denominator in figuring out this percentage was 25 percent smaller than that which the Department of Banking reported when the bank closed in 1931. By underreporting the total deposits and overreporting the dividends paid out, state officials were able to dress up the bleak record of their liquidation efforts in Toledo. When the figures are straightened out, the Security-Home depositors who held onto their claims until the bitter end actually recovered closer to 60 percent of their money.47

Of course, losses are computed not only in volume but in time, and Toledo’s bank liquidation took longer than any other in the state. The longer it takes for money to be recovered, the more is lost in the unearned utility of that money. The time in which those frozen deposits could have been used to purchase tools, to open a small business, to finance an education, or to make investments, could never be recovered. Even had the money never been touched, but simply left in a bank account, it would have gradually accumulated interest and grown. Of the last 5 banks to be liquidated out of the 211 banks closed in Ohio during the Great Depression, 3 were located in Toledo. Liquidation in Toledo did not officially come to an end until the spring of 1943, when the Commerce Guardian and the Ohio banks mailed their last dividends to depositors.48 Toledo’s long span of liquidation was the financial equivalent of an investment losing all its principal. Had the banks stayed open and people’s money simply sat in an account at an interest rate of 4.5 percent, compounding interest would have rewarded them with a 60 percent increase over their principal by 1941, about the same amount as the total recovered by general depositors of the Security-Home bank.

In the end, even using the Banking Department’s optimistic numbers, $5,780,806 in Security-Home deposits alone were never repaid, a sum alone equal to 22.4 percent of the losses across all 158 banks that had been liquidated in Ohio during the decade of the 1930s. Even without the addition of the losses at the three other big banks to the Security-Home’s total, Toledo’s losses dwarfed those of any other city in the state.

While the size of Toledo’s losses are explainable given the rottenness of the bank’s foundations before they failed and the scale of last-minute insider loans and withdrawals, the incredible duration of the liquidation in the city
is not. To some degree, the time it took to sell off the assets of banks was proportionate to their size. The mammoth state banks in Toledo simply had so many tens of thousands of lots, mortgages, securities, and buildings that to have dumped them all on the market at one time would have been impossible. But other large liquidations didn’t take quite as long. The Union Trust Company of Dayton, a bank about the same size as Toledo’s Commerce Guardian Bank, failed a month after the banks in Toledo but was fully dissolved nearly three years ahead of Toledo’s first bank to wrap up its business.\(^4^9\) One reason for the difference may have been that some people had an interest in prolonging the business of wrapping up the banks’ affairs.

Each year Toledo’s failed banks spent hundreds of thousands of dollars to pay for their own dismemberment. Some of this money went to cover the salaries of the hundreds of clerks, accountants, and secretaries retained by the banks. Other bills, such as for utilities, bank office mortgages, and administrative supplies, also had to be paid out of bank earnings and assets. But one of the biggest expenses was the legal costs incurred in both suing intransigent debtors and in fending off depositor and shareholder lawsuits. For a few well-placed legal firms in Toledo, the bank disaster was a huge source of revenue.

By one conservative estimate, about one hundred thousand dollars was paid to local law firms to handle various bank suits on behalf of the state during the first two years after the bank’s failure. Most of this money poured into the coffers of a handful of politically connected law firms at the discretion of the liquidation supervisors and the state’s Republican attorney general, Gilbert Bettman.\(^5^0\) With no public review of these appointments or their costs, they proved a great source of patronage and political favoritism. The bulk of the legal contracts went to the firm of Brown and Sanger, whose senior partner, Walter Folger Brown, still reigned as state GOP boss. Brown’s first lieutenant, N.J. Walinski, and the important chairman of the Lucas County Republican Central Committee, Nolan Boggs, also landed a share of fees. Smaller portions of the legal pie went to Lehr Fess, son of Republican Senator Fess, and to Duffey, Bryce and Duffey, the firm of Congressman Duffey. The attorney general’s office was aware that this was an uneconomical method of liquidation, for in the days immediately following the collapse of the banks its spokesman was quoted as saying that the AG’s office would “do everything possible to handle the legal work so that there would be no expense to depositors.”\(^5^1\)

With politics behind the commissioning of lawyers and no public accountability of their activities (as legal costs were not reported separately from all the other costs of liquidation) legal fees spiraled upwards. By the
second year of liquidation, even the attorney general’s office began to com-
plain that fees given to Toledo lawyers were inflated by half. Bank suits
proved such a steady source of income that in many cases lawyers initiated
suits and won judgments on behalf of bank liquidators who would not bother
to actually collect on them. In 1935, after depositors’ groups denounced
the filing of phony cases against bankrupt debtors by politically appointed
law firms, incoming Democratic governor Martin Davey announced he was
appointing a special investigator to look into the charges. Davey, eager to
pounce on an issue that could embarrass the previous administration, said,
“In Toledo, I am told, one lawyer was paid $60,000 from the assets of a sin-
gle closed bank. In numerous other cases money which should have been
distributed to distressed depositors was dissipated in attorney’s fees.” In some
cases, Davey said, this practice “took on the aspects of a regular racket.”

Little came of the Davey investigation, and apparently little changed in
the legal bonanza of liquidation in Toledo. Five years later the same depos-
itor activists were still denouncing the legal farming of banks for legal fees,
especially the practice of retaining lawyers who themselves owed large sums
of money to the banks. Judge John S. Pratt was paid a retainer by the Ohio
Bank of $500 per month although he owed the Ohio Bank $10,929. None
of Pratt’s salary was credited to his debt. This was particularly ironic as
it was reported that in the early months of the banks’ liquidation a num-
ber of law firms offered their services to the state Banking Department, ask-
ing that their fees be applied to debts they owed the closed banks. These
offers were turned down.

Because the Ohio Banking Department did not release itemized reports
of the expenses incurred in closing the banks in Toledo, it is impossible to
estimate the total amount overspent on legal expenses. However, the over-
all cost of liquidation in Toledo was so much higher than that in the state
as a whole that these expenses must have been quite large. By 1940, the
cost of liquidation of the four largest Toledo banks was $4,123,573. This
amounted to 6 percent of total deposit claims at these banks, a total twice
as large as the statewide average of 3 percent. Though Toledo accounted
for about one-tenth of all the deposits frozen in bank failures during the
decade of the 1930s, it used one-fifth of the total money spent to clean up
the mess.

The task of closing Toledo’s banks took more than a decade and millions
of dollars. Like the bank failures themselves, the bank liquidations were char-
acterized by insider favoritism, class privilege, and political patronage. Though
by 1941 the banks may have eventually paid out nearly as much money to
their creditors as they froze in 1931, much of it was funneled upwards to
the already wealthy and powerful while most humble depositors only ever
recovered a small fraction of their savings. For some, the liquidation of Toledo’s banks proved a boon rather than a bust. For most, the secrecy and unfairness that surrounded the process of liquidation merely confirmed all their worst assumptions about the lack of democracy in their community. While Toledo’s elites pecked at its financial corpses, masses of everyday depositors organized to demand justice.