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The Legal History of Safekeeping and Safe Deposit Activities in the United States

*Richard A. Lord**

I. INTRODUCTION

Today in the United States, bankers take for granted that the functions of banking include the safekeeping of customer valuables and the offering of safe deposit services. Virtually every commercial bank makes safekeeping and safe deposit services available, either through a department of the bank or through a subsidiary or affiliated safe deposit company. In some parts of the country, the demand for safe deposit facilities has led banks to increase the fees for safe deposit services and has revitalized an old industry: safe deposit companies whose sole function is the storage of documents, jewelry, coin and stamp collections, and other assorted valuables.

This article explores the legal history of safekeeping and safe deposit activities so that future problems that arise in connection with safe deposit services may be dealt with in a rational manner, consistent with historical developments.

II. A BRIEF OVERVIEW

Historically, the safekeeping function is perhaps the oldest function in banking,¹ having been performed by bankers and others in the community who were deemed worthy of the public's trust. Although there is little documented evidence, it appears that the first commercial banks in the American colonies engaged in safekeeping activities of some type and did so without explicit authority in their charters or by-laws.² Even

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1. G. MUNN, *ENCYCLOPEDIA OF BANKING AND FINANCE* 811 (7th ed. 1973); *AMERICAN INSTITUTE OF BANKING, PRINCIPLES OF BANK OPERATIONS* 272 (1966); N. HOGGSON, *BANKING THROUGH THE AGES* 33-43 (1926).

2. See 1825 N.Y. Laws 204-210; 1825 N.Y. Laws 198-201; 1838 N.Y. Laws 245-253.

the National Currency Act of 1864³ did not provide for the conduct of safekeeping or safe deposit activities by national banks, although banks apparently engaged in such activities and were implicitly authorized to do so by the National Currency Act's proscription of any activity not incidental to banking.⁴

By the mid-1800's, safe deposit corporations began to be formed, partly because of scientific advances, partly to compete with banks, and partly because the safekeeping function of banks had never been particularly profitable.⁵ Often a bank would agree to safekeep a customer's personalty at little or no cost. Moreover, even the rental of safe deposit boxes was for a modest fee, which did not reflect the true cost of the department. Safekeeping and safe deposit functions were performed almost purely as a service to the customer, occasionally gratuitously, but more often for a nominal fee, and, in either event, were truly incidental to the business of banking.⁶

The fact that safe deposit and safekeeping services were incidental to the business of banking, although earlier recognized by the states,⁷ was not explicitly recognized by Congress until 1927 when it enacted the proviso to section 24 of the National Bank Act.⁸ Even that legislation did not explicitly confer upon national banks the right to engage in the safe deposit business. Rather, it permitted national banks to invest in safe deposit companies.

The dual nature of our banking system has always cre-

3. First codified in 18 Stat. Title LXII §§ 5133-5234 (1878); codified today as The National Bank Act, 12 U.S.C. § 38 (1982). That banks did engage in safekeeping activities is clear from the early cases, *see, e.g.*, *Roberts v. Stuyvesant Safe Deposit Co.*, 123 N.Y. 57, 25 N.E. 294, *reh'g denied*, — N.Y. —, 25 N.E. 955 (1890); *Safe Deposit Co. v. Pollock*, 85 Pa. 391, (1878).

4. 18 Stat. Title LXII § 5136 (1878). To the extent that banks were engaged in safekeeping activities at the time of the National Bank Act's passage, which is clear from the case law, Congress must have considered this function incidental to the business of banking or the activity would have been proscribed.

5. McBain, *Safe Deposit Department*, 72 BANKING L.J. 533 (1955).

6. *Id.* at 534.

7. *See* 2 PATON'S DIGEST 2246-48 (1926). *See also* *Colorado Nat'l Bank v. Bedford*, 340 U.S. 41, 49-50 (1940).

8. 12 U.S.C. § 24 (1982).

ated competitive tension between state and national banks.⁹ Thus, to the extent that state banks were permitted to and in fact did engage in safe deposit and safekeeping activities, national banks were sure to follow. Beginning around the 1900's, some state banks were granted explicit authority to engage in safe deposit activities.¹⁰ Moreover, a number of banks, both state and national, took for granted that they were entitled to engage in safe deposit activities. Thus, there are indications that safe deposit activities in the 1920's were regularly being performed by national banks.¹¹ However, it was not until the late 1930's that the courts decided the issue of whether a national bank could engage in safe deposit activities as incidental to the business of banking.¹²

It is well settled today that both state and national banks may engage in safe deposit activities. The state authority to engage in such activities varies from explicit authority, such as that found in New York, New Jersey and Michigan;¹³ to general authority permitting state banks to engage in activities that are incidental to the business of banking, such as that found in Alabama, North Carolina, and Wyoming;¹⁴ to authority that permits state banks to engage in activities which national banks may engage in, such as that found in Arizona and North Dakota;¹⁵ to implied authority, where the reference to safe deposit boxes in state statutes implies that they must be

9. See Hackley, *Our Baffling Banking System*, 52 VA. L. REV. 565 (1966); Leavitt, *The Philosophy of Financial Regulation*, 90 BANKING L.J. 632 (1973); Redord, *Dual Banking: A Case Study in Federalism*, 31 LAW & CONTEMP. PROBS. 749 (1966).

10. See *supra* note 7. See also COLO. REV. STAT. § 11-9-102 (Supp. 1983); N.Y. BANKING LAW § 96(3)(b) (McKinney 1971). Both are codifications of much earlier statutory enactments.

11. "The obvious fact, known to all, is that national banks do and for many years have carried on a safe-deposit business." *Colorado Nat'l Bank v. Bedford*, 310 U.S. 41, 49 (1940). See also *Roberts v. Minier*, 240 Ill. App. 518 (1926); *Young v. First Nat'l Bank of Oneida*, 150 Tenn. 451, 265 S.W. 681 (1924); *McDonald v. Perkins & Co.*, 133 Wash. 622, 234 P. 456 (1925).

12. *Bank of Cal. v. City of Portland*, 157 Ore. 203, 69 P.2d 273 (1937), *cert. denied*, 302 U.S. 765 (1938).

13. N.Y. BANKING LAW § 96(3)(b) (McKinney, 1971); N.J. STAT. ANN. § 17:9A-24 (West 1984); MICH. COMP. LAWS § 487.488 (1970).

14. ALA. CODE § 5-5A-18(11) (Repl. 1981); N.C. GEN. STAT. § 53-43(1) (Repl. 1982); WYO. STAT. § 13-2-101 (1977).

15. ARIZ. REV. STAT. ANN. § 6-184 (Supp. 1984); N.D. CENT. CODE § 6-03-38 (Repl. 1975).

permitted.¹⁶ With respect to national banks, the authority derives from the powers incidental to the business of banking.¹⁷ There is, however, specific statutory authority, such as that contained within the proviso to section 24, which impliedly permits banks, or explicitly authorizes their affiliates or subsidiaries, to engage in safe deposit activities.

More often than not, safe deposit activities in the past have been undertaken by a department within the bank, rather than through an affiliate or subsidiary. This practice was largely due both to the fact that safe deposit activities were conducted as a non-profit-making activity as well as the fact that the demand for safe deposit services was not as great as the supply of safe deposit facilities. Thus, it made no sense to engage an affiliate or a subsidiary. It is likely, however, that the future will see greater numbers of banks (and bank holding companies) engaging in safe deposit activities through subsidiaries.

Although banks historically have been the primary provider of safe deposit services, the increase in personal wealth has provided an incentive for the creation of new safe deposit companies. While safe deposit companies themselves are not a new phenomenon, particularly in large urban areas,¹⁸ their size and numbers will likely grow in the future. On the whole, their rights and responsibilities are essentially the same as those of banks, at least insofar as safe deposit activities are concerned.¹⁹

III. HISTORICAL ANTECEDENTS

A. The Pre-Colonial History of Safekeeping Activities

The history of safekeeping activities is the history of

16. ALA. CODE § 5-5A-18(11) (Repl. 1981); CAL. FIN. CODE § 757 (West 1968).

17. 12 U.S.C. § 38 (1982); see *Bank of Cal. v. City of Portland*, 157 Ore. 203, 69 P.2d 273 (1937), *cert. denied*, 302 U.S. 765 (1938); see also G. MUNN, *ENCYCLOPEDIA OF BANKING AND FINANCE* 811 (7th ed. 1973).

18. See *Banks as Lessors of Safe Deposit Boxes*, 18 *BANKING L.J.* 770 (1901); Hodge, *Law of Safe Deposit*, 3 *DET. L. REV.* 69 (1933); Hatch, *Safe Deposit History*, *THE SAFE DEPOSIT BULL.* (June 1931).

19. *Safe Deposit Co. v. Pollock*, 85 Pa. 391 (1878); *Cussen v. Southern Cal. Savings Bank*, 133 Cal. 534, 65 P. 1099 (1901); *Schaefer v. Washington Safety Deposit Co.*, 281 Ill. 43, 117 N.E. 781 (1917).

banking itself. In ancient Egypt and Babylon, individuals who occupied positions of trust in the community were entrusted with the valuables of others, usually for a fee, under circumstances resembling our modern banking practices.²⁰ Later, the ancient Greeks discovered that their temples provided a safe haven for valuables, and it is perhaps there that the first true equivalent of the modern safe deposit vault existed.²¹ Originally, the services were gratuitous, but eventually safekeeping services became part of the established business of banking, and uniform changes coupled with complete record-keeping became the norm.²²

In each succeeding civilization from that time until today, the need for banks became quickly apparent. Just as trade and commerce necessitated banks, the wealth brought about by such trade and commerce necessitated safe places for the storage of that wealth. The banks, charged with other financial responsibilities, became an obvious storage house for the valuables of their customers.

B. The Colonial History of Safekeeping Activities

On our own continent, during the colonial period, smiths and other businessmen performed the safekeeping function rather than banks, for banks were, initially, nonexistent. In colonial days, as elsewhere throughout history, commerce was originally transacted by means of barter. There was little precious metal wealth, and that which was considered valuable in terms of trade, such as tobacco, corn, and beaver pelts,²³ was not susceptible to safekeeping. Further, although wampum was capable of storage, it was not monetized except in terms of pure barter. Thus, the colonists, though "wealthy," did not have enormous wealth of the sort that had to be safekept.

As the colonies developed, and trade became more so-

20. N. HOGGSON, *BANKING THROUGH THE AGES* 33-34 (1926); *See also* *Bank of Cal. v. City of Portland*, 157 Or. 203, 69 P.2d 273 (1937), *cert. denied*, 302 U.S. 765 (1937).

21. N. HOGGSON, *BANKING THROUGH THE AGES* 33-34 (1926).

22. *Id.* at 34-35.

23. J. WHITE, *TEACHING MATERIALS ON BANKING LAW* 1 (1976); P. STUDENSKI AND H. KROOS, *FINANCIAL HISTORY OF THE UNITED STATES* 12-13 (2d ed. 1963).

phisticated, money systems were developed. Thus, in the hundred years beginning around 1650 and ending in approximately 1750, colonial mints for the coinage of gold, silver, and copper were established, and paper money made its appearance.²⁴ British reaction was predictable; by the mid-1700's, coinage and production of paper money were prohibited by the Crown.²⁵ The prohibition was to a large extent ignored, and the colonists formed banks for the purpose of continuing the production of paper money.²⁶ This money was used in trade, and for the primary purpose of purchasing land,²⁷ so the colonists were still without substantial wealth of the sort that would require safekeeping, and the "banks" therefore did not perform safekeeping functions with any significant regularity.

C. Early American Safekeeping Activities

Following the American Revolution, it became apparent to the new American governors that one or more banks would be required. The public, however, distrusted banks, largely as a result of the depreciated money that had been printed preceding and during the War of Independence. Nevertheless, formal banks were recognized as necessary to facilitate trade and commerce, and the first American commercial bank, the Bank of North America, was founded in 1782.²⁸ Not surprisingly, the Bank of North America's charter did not make any mention of safekeeping activities. Although the grant of power contained within the congressional charter was probably sufficiently broad to encompass safekeeping activities,²⁹ they were by no means specifically permitted. There were two reasons for this omission: first, the need for safekeeping serv-

24. P. STUDENSKI AND H. KROOS, *FINANCIAL HISTORY OF THE UNITED STATES* 14-15 (2d ed. 1963).

25. *Id.* at 14-15, 17.

26. *Id.* at 15.

27. *Id.* at 15-16.

28. *Id.* at 31; see also Symons, "The Business of Banking" in *Historical Perspective*, 51 *GEO. WASH. L. REV.* 676, 686 (1983); Lord, *The No-Guaranty Rule and the Standby Letter of Credit Controversy*, 96 *BANKING L.J.* 46, 48 (1979); P. STUDENSKI & H. KROOS, *supra* note 24, at 31; J. WHITE, *supra* note 23, at 2.

29. M. CLARKE & D. HALL, *LEGISLATIVE AND DOCUMENTARY HISTORY OF THE BANK OF THE UNITED STATES* 2-13, 14-35 (1832).

ices was not yet great; and second, backers of the bank were more concerned with its survival than with exercising incidental powers. However, the bank not only survived, it flourished.

Shortly after the successful establishment of the Bank of North America, the Bank of New York and the Bank of Massachusetts were formed, each having as its main object the performance of a traditional banking business in a major American city (New York and Boston). Like the Bank of North America—which had since become a state chartered bank in Pennsylvania³⁰—the Bank of New York and the Bank of Massachusetts were both permitted to exercise broad powers by their charters and regulations.³¹ Nevertheless, there was no specific mention of the safekeeping function.

These initial ventures into banking were so successful that, by 1800, almost thirty banks existed throughout the country,³² and ten years later, almost one hundred banks existed.³³ Despite the rapid growth of the banking business, there is no indication that any of these banks were authorized to perform a safekeeping business. Although all of the charters have not been reviewed, the state laws pursuant to which the charters were issued have been, and it is clear that in none of the state laws was there specific authority to engage in safekeeping activities. Nevertheless, these activities were already an established part of the young banking industry in this country. Thus, it is apparent that in the period between the Revolution and the War of 1812 the newly formed banks began to respond to the need of their customers for safekeeping services. The apparent reasons were the expansion of trade, the development of one or more stable currencies, and the growth of individual wealth, particularly among the traders.

This conclusion is made explicit by the early landmark decision of *Foster v. Essex Bank*,³⁴ decided by the Supreme

30. J. WHITE, *supra* note 23, at 2; P. STUDENSKI & H. KROOS, *supra* note 24, at 32.

31. Those regulations later became N.Y. BANKING LAW § 106(5) (McKinney 1921); MASS. GEN. LAWS ANN. ch. 79 (West 1921).

32. P. STUDENSKI & H. KROOS, *supra* note 24, at 73 n.12.

33. *Id.* at 73; J. WHITE, *supra* note 23, at 8 (75 state banks).

34. 17 Mass. 479, 9 Am. Dec. 168 (1821).

Court of Massachusetts in 1821. The case dealt with a "special deposit" of approximately \$50,000 in gold that had been left by one Israel Foster. Foster brought the money to the bank for safekeeping and received a receipt indicating the deposit. Sometime later, the cashier and clerk of the Essex Bank absconded with this and other monies. The executors of Israel Foster's estate brought suit against the bank to recover \$50,000.

The importance of the case lies in its recognition of the fact that banks engaged regularly in the receipt of special deposits. The court noted:

The practice of receiving [special deposits for safekeeping] must have originated in a willingness to accommodate members of the corporations with a place for their treasures, more secure from fires and thieves than their dwelling-houses or stores; and that is rendered more probable from the well-known fact, that not only money or bullion, but documents, obligations, certificates or public stocks, wills and other valuable papers, are frequently, and in some banks as frequently as money, deposited for safe keeping. This is wholly different from the deposits contemplated in the act on which notes may be issued, for they enter into a capital stock, become the property of the bank, as much as their other moneys, and the bank become debtors to the depositors for the amount.³⁵

It is clear from the *Essex* case that most banks engaged in the receipt of special deposits for safekeeping purposes as early as the early-1800's. The safekeeping deposit in that particular case had been made prior to 1814. According to the court, the bank was not specifically authorized to accept special deposits for safekeeping, either by the act pursuant to which it was incorporated or by its internal charter, rules, or regulations:

[N]otwithstanding the act of incorporation gives no particular authority or power to receive special deposits, and although the verdict finds that there was no regulation or by-law relative to such deposits, or any account of them required to be kept and laid before the directors or

35. *Foster*, 17 Mass. 479, —, 9 Am. Dec. 168, 177 (1821).

the company, or any practice of examining them; yet as it is found that the bank, from the time of its incorporation, has received money and other valuable things in this way, and as the practice was known to the directors, and, . . . as the building and vaults of the company were allowed to be used for this purpose, and their officers employed in receiving into custody the things deposited, the corporation must be considered the depositary³⁶

The questions presented for the court were whether the bank should bear responsibility for the act of its agent and the degree of care to which it would be held responsible.³⁷ The safekeeping at issue was gratuitous. In that respect, it differed from the modern safe deposit or safekeeping function. Nevertheless, the *Essex* case clearly demonstrates that this form of safekeeping activity was well recognized and established in the formative period of our country.

D. Early Federal Authority to Engage in Safekeeping Activities

In 1864, Congress passed the National Currency Act, which was the forerunner to and embodied many of the provisions of the National Bank Act. That statute provided that national banks could engage in activities that were incidental to the business of banking. Moreover, one section provided that, upon the insolvency of a bank, it could no longer engage in the business of banking except, among other things, to deliver special deposits which had been entrusted to it.³⁸ Although one might have asked for a more explicit grant of authority, the statute certainly suggested that banks were permitted to take special deposits. Since banks were given specifically enumerated powers, which did not include the power to take special deposits, and since they were given additional general powers necessary to conduct the business of banking, and since another section presupposed the existence of special

36. *Id.* at 170.

37. The points raised are to some extent unsettled even today. See Lord, *The Legal Relationship Between the Bank and Its Safe Deposit Customer*, 5 CAMP. L. REV. 263 (1983).

38. Section 46 of the National Currency Act, currently found in the National Bank Act, 12 U.S.C. § 38 (1982).

deposits, it certainly appeared as though special deposits were "incidental to the business of banking."

The *Essex* case suggests that it had long been the custom of banks to receive special deposits, even before the apparent authority to receive the deposits was granted by the Act of 1864. The Massachusetts court that decided *Essex* forty years earlier was generally considered to be one of the leading courts of its day.³⁹ In fact, the *Essex* decision put an end for a while to the question of whether a bank could engage in the safekeeping function—most bankers and lawyers apparently reading the decision to establish safekeeping as incidental to the business of banking. Given that, and the fact that the Act of 1864 at least strongly suggested that the safekeeping function was incidental to the business of banking, it was to be expected that the question would forever be put to rest. However, exactly the opposite was true; the question began to be litigated with increasing frequency.

One can only speculate as to the reasons for the increased litigation concerning whether banks had authority to engage in the safekeeping of their customer's valuables. There appear to have been at least three reasons. First, the passage of the 1864 Currency Act gave rise to an argument based upon the distinction between state and national banks. The *Essex* decision had dealt with state banks, for only state banks had existed to any significant degree prior to the mid-1860's. Following the enactment of the National Currency Act, which provided for the chartering of national banks, there was a concerted effort to eliminate state chartered banks and a concomitant effort to charter national banks.⁴⁰ Thus, it could be argued that *Essex* established a particular proposition for state banks and that the Currency Act established a new category of banks to which different rules might apply. In this connection, it must be borne in mind that the Essex Bank did not

39. See, e.g., another opinion written by the court on safe deposits, *Bottom v. Clarke*, 61 Mass. (7 Cush.) 487 (1851). See also J. WHITE, *THE REGULATION AND REFORM OF THE AMERICAN BANKING SYSTEM* 25 (1983); J. WHITE, *supra* note 23, at 18-19.

40. See Symons, *supra* note 28, at 699. Some believe that this effort was solely that of Salmon P. Chase, Secretary of the Treasury at the time. See J. WHITE, *supra* note 23, at 18-19.

appear to have regulations imposed upon it or enacted by it; the National Currency Act specifically enumerated certain powers and allowed for the conduct of other general activities incidental to banking. Thus, a theoretical distinction existed because national banks could only do what the National Act permitted.

Second, the doctrine of *ultra vires*, which predated the existence of the United States, was developing with regard to banks at approximately this time. To the extent that banks were being developed as modern corporations, corporation law doctrines such as *ultra vires* were being tested as applicable. While it has been suggested that the courts have always distinguished between banks and other corporations, the distinction has not always been well articulated.⁴¹ In fact, the probability is "that when banking was developing in this country, its corporate identity was viewed as being comparable to that of any corporation."⁴² Thus, when banks were sued for having lost safekept property, they invariably responded with one of two arguments: first, that it was beyond the power (*ultra vires*) of a bank to safekeep a customer's property, and therefore the bank could not be liable;⁴³ or second, that the teller or other officer receiving the property lacked authority to bind the bank.⁴⁴ Both of these doctrines, broadly applicable to corporations in general, were raised by banks to escape liability. It is interesting to note that the banks were less successful here than they have been in other areas.⁴⁵ Nevertheless, the insistence by banks that they lacked

41. Lord, *The No-Guaranty Rule and the Standby Letter of Credit Controversy*, 96 BANKING L.J. 46, 54-55 (1979).

42. *Id.* at 55; See also Symons, *supra* note 28, at 686-88. *State v. Kelsey*, 53 N.L.J. 590, 22 A. 342 (1891); *N.J. Title & Trust Co. v. Rector*, 76 N.J. Eq. 587 (1910).

43. See, e.g., *Pattison v. Syracuse Nat'l Bank*, 80 N.Y. 82, 36 Am. Rep. 582 (1880); *Foster v. Essex Bank*, 17 Mass. 479, 9 Am. Dec. 168 (1821); *Third Nat'l Bank v. Boyd*, 44 Md. 47, 72 Am. Rep. 35 (1876).

44. See *Foster v. Essex Bank*, 17 Mass. 479, 9 Am. Dec. 168 (1821); *Scott v. Nat'l Bank of Chester Valley*, 72 Pa. 471, 13 Am. Rep. 711 (1874); *Lancaster County Nat'l Bank v. Smith*, 62 Pa. 47 (1869).

45. See *Safe Deposit Co. v. Pollock*, 85 Pa. 391, 27 Am. Rep. 660 (1878); *Lockwood v. Manhattan Storage & Warehouse Co.*, 28 A.D. 68, 50 N.Y.S. 974 (1898); *Cussen v. Southern California Sav. Bank*, 133 Cal. 534, 65 P. 1099 (1901); *Tacoma Park Bank v. Abbott*, 19 A.2d 169 (Md. 1941); Taylor, *Legal Considerations Affecting Safe Deposit Practices*, 74 BANKING L.J. 751, 755 (1957); Note, *Liability of Lessors of Safe*

the power to safekeep property almost certainly fueled litigation.

The third reason for the increased litigation concerning the banks' authority to safekeep customer valuables had little to do with banking as such. Rather, it had to do with technological innovation in the form of the invention, in the 1860's, of the modern safe deposit box.⁴⁶ This ingenious device revolutionized safekeeping, for it became possible for a customer to place valuables in a sealed container, obtain individual access, and yet store this sealed container within a safe or vault. It became less important who had access to the vault area, since, without the individual customer's key, it was impossible (absent violent means) to enter the safe deposit box of a particular individual. Thus, the character of the vault became more important than the character of the individual guarding or maintaining the vault.

One result of this technological development was that safe deposit companies began to be formed for the express purpose of storing the valuables and documents of individuals. The first of these safe deposit companies was organized in 1865,⁴⁷ and safe deposit companies were soon formed in the major cities.⁴⁸ The result was not only to give rise to competition between safe deposit companies and banks but also to call into question the legitimacy of the safekeeping function as incidental to the business of banking. That question therefore became ripe for consideration by the courts.

Beginning around 1870, the appellate courts heard cases dealing with the issue of whether national banks could engage in safekeeping. Most of the decisions cited *Essex* with approval.⁴⁹ Only in Vermont was a contrary result reached, in

Deposit Boxes, 7 MD. L. REV. 76, 80 (1942); Lord, *The No-Guaranty Rule and the Standby Letter of Credit Controversy*, 96 BANKING L.J. 46 (1979). Symons, *supra* note 28, at 701-14.

46. This invention was a "comparatively late development in American Banking." G. MUNN, *ENCYCLOPEDIA OF BANKING AND FINANCE* 811 (7th ed. 1973).

47. *Id.*; Taylor, *supra* note 45.

48. MUNN, *supra* note 46; *Banks as Lessors of Safe Deposit Boxes*, *supra* note 18, at 771.

49. See, e.g., *Scott v. Nat'l Bank of Chester Valley*, 72 Pa. 471 (1874); *Turner v. First Nat'l Bank of Keotuck*, 27 Iowa 562 (1869); *Smith v. First Nat'l Bank of Westfield*, 99 Mass., 605 (1868); *Lancaster County Nat'l Bank v. Smith*, 62 Pa. 47 (1869);

Wiley v. First National Bank of Brattleboro,⁵⁰ where the court declined to adopt the *Essex* rationale:

[In *Essex*] it was decided that, on account of that practice, and not because it was a part of legitimate banking business, the bank became charged with the liabilities of a depository of the coin. . . . no other case as to the scope of the powers of banks . . . appears to have arisen and been decided between that and the passage of the Act of Congress in 1864, under which this bank was organized.⁵¹

The *Wiley* court determined that the business of receiving special deposits was not incidental to the business of banking but was more incidental to the business of warehousing. Applying the rule *expressio unius est exclusio alterius* (the mention of one excludes all others), the court held that the National Currency Act did not authorize the receipt of special deposits. Furthermore, to the argument that the mention of special deposits elsewhere in the National Currency Act implied that banks might receive them, the court responded that that section was intended not to add powers, but to restrict them. In fact, the *Wiley* court explicitly declared that the chief difference between *Wiley* and *Essex* was the fact that, in *Essex*, the charter did not expressly stipulate what banks could do, whereas the National Currency Act did. The failure to include special deposits among the enumerated powers was fatal.

The courts of the time apparently took *Essex* to mean at least that a state bank, even if it could not properly take special deposits, would be estopped from denying liability in the event that it did take a special deposit with the approval of its directors.⁵² The same courts apparently believed that *Wiley* stood for the proposition that a national bank was not empowered to take gratuitous special deposits. And, if it did, the

First Nat'l Bank of Carlisle v. Graham, 79 Pa. 106 (1879); Chattahoochee Nat'l Bank v. Schley, 58 Ga. 369, 198 S.E. 559 (1877).

50. 47 Vt. 546 (1875); See also Whitney v. First Nat'l Bank of Brattleboro, 50 Vt. 389 (1877).

51. Wiley v. First Nat'l Bank of Brattleboro, 47 Vt. 546, 553 (1875).

52. Lancaster County Nat'l Bank v. Smith, 62 Pa. 47 (1869); Scott v. Nat'l Bank of Chester Valley, 72 Pa. 471 (1874); Smith v. First Nat'l Bank of Westfield, 99 Mass. 605 (1868).

cashier who took them became solely responsible. Certainly, the highest courts in the states of Maryland and New York, two jurisdictions significantly more commercially important than Vermont, believed that *Wiley* stood for that proposition. Thus, in *First National Bank v. The Ocean National Bank*,⁵³ the Court of Appeals of New York indicated quite strongly in dictum that the taking of special deposits was not an incident of banking. The court expressed its doubts, indicating that the bank's powers were

banking powers only, with such incidental powers as may be necessary to carry on the business of banking, with the privilege of buying and selling exchange, coin and bullion. This does not necessarily include the business of a safe deposit company, or [the] business of receiving for safe keeping, and storing for hire, or without compensation, jewelry and valuables, or property of any kind. If the power exists in the corporation as part of its franchise, it is only as an incident of its principal business.⁵⁴

* * * *

The deposit of these bonds cannot be distinguished from a deposit of jewelry or plate, or other valuable property, and was a special transaction not within the ordinary course and business of banking, or necessarily incident to it.⁵⁵

The New York court distinguished the *Essex* case on the basis of the acquiescence of the directors and then made clear that, since there had been no acquiescence in the case before it, there was no reason to determine whether the bank had the power to receive special deposits.⁵⁶ However, during the time between the writing of the decision and its publication, the court was made aware of the *Wiley* case. That fact led the New York Court of Appeals to observe:

[*Wiley*] held that the cashier of a national bank has no power to receive special deposits in behalf of the bank for the accommodation of the depositor, or to bind the bank to any liability on any express contract accompanying, or any implied contract arising out of such taking, and the

53. 60 N.Y. 278 (1875).

54. *Id.* at 287.

55. *Id.* at 289.

56. *Id.* at 294.

judgment is sustained by a well-considered opinion. . . .
In his views I fully concur.⁵⁷

This decision apparently placed New York, one of the premier commercial states in the country, in the camp of those who argued strenuously that national banks—or for that matter, any banks—did not have the power to receive special deposits. Such a decision virtually ignored a number of other cases which had implicitly recognized the ability of national banks to take special deposits,⁵⁸ as well as the language of section 46 of the National Currency Act (which permitted banks, upon insolvency, to pay special deposits). Moreover, it placed *Essex* into that category of cases which determined that only if a bank's directors acquiesced in a course of conduct could the bank be responsible. *Essex* was no longer the leading case on the question of whether a bank could take special deposits; rather it became a leading case on estoppel or acquiescence for purposes of corporate ratification. Moreover, *Wiley*, which had not sought to distinguish *Essex* on this ground alone, but which seemed to repudiate it on an *exclusio unius* basis, became transformed into the leading case. It quite clearly stood for the proposition that national banks had no power to receive special deposits.

On the heels of the *Ocean National Bank* case came the decision in *Third National Bank v. Boyd*.⁵⁹ The Court of Appeals of Maryland had before it the issue of whether a national bank had the power to take and hold certain stocks and bonds which had originally been deposited as collateral for a loan, when the loan had been fully discharged. The stocks and bonds had been deposited with the bank as collateral for the bank's ongoing lending to Boyd. Very often, however, and for substantial periods of time, Boyd would not owe the bank any money, and yet the bank would maintain his bonds in its vault. During one such period, the bank was robbed, and the

57. *Id.*

58. *Turner v. First Nat'l Bank of Keokuk*, 26 Iowa 562 (1869); *Smith v. Nat'l Bank of Westfield*, 99 Mass. 605 (1868); *Lancaster Co. Nat'l Bank v. Smith*, 62 Pa. 47 (1869).

59. 44 Md. 47, 22 Am. Rep. 35 (1876).

bonds were stolen. The plaintiff brought suit against the bank to recover the value of the bonds.

The bank defended on, among other grounds, the basis that it was beyond its power to take special deposits gratuitously or for hire. The court, in dictum, agreed:

There is very strong ground, both upon reason and authority, in support of the proposition that a National Bank, deriving its existence and exercising its powers under the Act of Congress referred to, is not authorized to enter into a contract as a mere gratuitous bailee, by receiving on special deposit for safe-keeping merely, coin, jewelry, plate, bonds or other valuables. Such a contract does not appear to be authorized by the terms of [the Act] as a transaction "within the ordinary course and business of banking or incident to it;" and has been decided by [the *Wiley* court] to be unauthorized by law, and beyond the scope of the corporate powers.⁶⁰

The Maryland court also cited the *Ocean National Bank* case and specifically assumed that both of those cases were correct.⁶¹ The court held, however, that the deposit was not a mere special deposit because the original contract was for the bank to take the stocks and bonds as collateral. The fact that no debt was currently owed did not change the original character of the deposit, which was one for security.

Thus, by 1875, the legitimacy of national banks receiving special deposits was called into question by the courts of at least three states, including two of the most well-respected commercial states. The *Essex* decision, rendered fifty years earlier by an equally important commercial state, Massachusetts, had been largely discredited for its main proposition, although followed regularly for other propositions. What had seemed so clear in 1821, on the basis of centuries old practices, was now called into serious doubt.

These decisions were the result of banks urging *ultra vires* when special deposits they had taken could not be returned to the depositors. It was now apparent that in all jurisdictions a bank which did not regularly take special deposits could not

60. *Third Nat'l Bank v. Boyd*, 44 Md. 47, 61, 22 Am. Rep. 35, 39 (1876).

61. *Id.* at 62, 22 Am. Rep. at 39.

be held liable, but more than that could not be said. A split apparently existed beyond that issue, with some courts citing *Essex* for the proposition that banks could take special deposits, others citing it for the proposition that they could be estopped from denying their ability to take special deposits, and others flatly disagreeing with *Essex*. In addition, a number of cases existed where, although the issue should have been addressed, it was not. Given that, prudent bankers should have refused to accept special deposits or, if they accepted them, should have done so knowing they were leaving their banks open to liability. Unfortunately, the information that was available to bank attorneys, and perhaps even to bank officers, apparently did not reach cashiers and clerks. The cases indicate quite clearly that the cashiers, clerks, and tellers continued to take special deposits (although the cases also indicate that very often they did not take them without first objecting to taking them, and then only upon a clear statement of nonliability). Thus, cases where special deposits had been taken and subsequently not redelivered continued to arise, and the bank-defendants in those cases continued to plead *ultra vires*.

In two such cases, decided at approximately the same time, the courts, for the first time, squarely addressed the issue of whether national banks could receive special deposits. The reason for considering this question, which had been considered only in dictum earlier, is not at all clear. It does appear, however, that the attorneys for the respective banks in these two cases argued more vigorously than they had earlier that the banks were without power to engage in safekeeping. The apparent reason for this was that in both cases a pattern of acquiescence had been engaged in, and gross negligence had been found. Thus, the only question at issue was whether a national bank had the power to engage in safekeeping or could be estopped from denying such power.

The two cases were proceeding through the court systems of Pennsylvania and New York at approximately the same time. The New York case, *Pattison v. Syracuse National Bank*,⁶² was decided by the New York Court of Appeals

62. 80 N.Y. 82, 36 Am. Rep. 582 (1880).

shortly before the United States Supreme Court decided *National Bank v. Graham*.⁶³ The Supreme Court cited *Pattison* with approval, and *Pattison* had in turn cited the Pennsylvania Supreme Court's opinion in the *Graham* case. Both of these decisions irrevocably determined that national banks had the power to engage in safekeeping activities.

In *Pattison*, the New York Court of Appeals traced the cases dealing with special deposits that had arisen both prior to and after the passage of the National Currency Act. The court noted that in many cases the corporate power to engage in safekeeping had not been made an issue and then discussed the cases wherein the issue had been raised, beginning with *Foster v. Essex Bank*. Noting that the bulk of the decisions had cited *Essex* with approval, the court returned its attention to the three jurisdictions where *Essex* had apparently not been approved: Vermont, Maryland, and New York. The court first indicated that *Wiley* was the only case which squarely decided the issue contrary to *Essex*. It then noted that the *Ocean National Bank* case had approved of *Wiley* only in dictum, and then by a minority of the court. The *Pattison* court made clear that the dictum of *Ocean National Bank* did not have basis in law or history, noting that historically, the earliest function of banking was that of safekeeping. On these bases, the New York Court of Appeals, perhaps the most influential commercial court in the country at the time, succinctly held: "On the question of corporate power, we are therefore of the opinion that National banks have power to receive special deposits, gratuitously or otherwise, and that when received gratuitously they are liable for their loss by gross negligence."⁶⁴

The decision of the United States Supreme Court in *Graham*, of course, was to be the final word on the subject. In that case, the plaintiff had, beginning in 1867, deposited bonds with the defendant bank for safekeeping. The cashier cut off and redeemed coupons for the plaintiff and deposited the proceeds in the plaintiff's account with the bank. The directors knew of the deposit, and the deposit for safekeeping was gra-

63. 100 U.S. 699 (1880).

64. *Pattison v. Syracuse Nat'l Bank*, 80 N.Y. 82, 97, 36 Am. Rep. 582, 590 (1880).

tuitous. The plaintiff sued when the bonds were allegedly stolen, and the bank urged a charge to the jury that national banks were not authorized to receive deposits for safekeeping and that the cashier had acted without authority and could therefore not bind the bank. The lower court instead charged the jury that if the officers and directors acquiesced in the safekeeping, and the bank were negligent, the plaintiff could recover. The jury returned a verdict for the plaintiff which, according to the United States Supreme Court, conclusively established the acquiescence and gross negligence.⁶⁵

The Supreme Court began its consideration of the issues raised by assuming that the contract was illegal as a result of *ultra vires*. It nevertheless indicated that the rule established by *Essex* would be applied with respect to national banks.⁶⁶ Referring to *Wiley* (and a subsequent Vermont decision, *Whitney v. First National Bank of Brattleboro*)⁶⁷ as the only direct authority to the contrary, the Court indicated that, given the acquiescence and the conclusive determination of gross negligence, the bonds involved were the responsibility of the bank and not the cashier alone. The Court, however, decided the issue on "another ground free from doubt."⁶⁸ That ground was the unquestioned authority of national banks to engage in safekeeping activities.

The Court first explored section 46 of the 1864 Act, which indicated that on default, banks could pay out special deposits. The implication existed that national banks could receive special deposits, an implication which, according to the Court, was the same as an express declaration of that fact. The Court next determined that a special deposit existed in the case before it, citing the *Pattison* case. It then concluded that national banks could receive special deposits "either on a

65. "The jury was instructed that . . . 'plaintiff's bonds were received for safe-keeping with the knowledge and acquiescence of the officers and directors of the Bank, and that if the bonds were lost by the gross negligence of the bank and its officers the Bank was liable.' [T]he jury thus found and affirmed the facts of knowledge and gross negligence by the Bank. These points are, therefore, conclusively established. . . ." *Graham*, 100 U.S. at 701.

66. *Id.* at 702.

67. 50 Vt. 388 (1877).

68. *Graham*, 100 U.S. at 703.

contract of hiring or without reward”⁶⁹ and that liability for negligence would flow from the safekeeping activities.

The *Graham* case established conclusively that national banks could engage in safekeeping activities. It did so primarily on the basis that had been urged in prior cases, including *Wiley*, *i.e.*, that the inclusion of a reference to special deposits elsewhere in the National Currency Act implied that national banks could engage in safekeeping activities. This basis foreshadowed what was to become the rule fifty years later relative to safe deposit services.

The *Pattison* case, on which *Graham* relied in part, did more than merely signal the direction that the Supreme Court would take. While it is true that *Pattison* placed New York squarely in line with the *Essex* decision, the case is important for at least two other reasons. First, the indications are quite strong that the National Currency Act would be interpreted so as to effectuate competitive equality between national and state banks. Such an interpretation accords well with historical notions of our dual banking system.⁷⁰ Second, it suggests the actual role that was being played by the developing safe deposit companies. As to the first matter, the *Pattison* court made abundantly clear its thought that, regardless of whether a bank’s charter was state or national, the question of the bank’s power to receive special deposits and engage in safekeeping would be answered the same.⁷¹ Thus, *Pattison* must have appeared to establish not only that national banks operating in New York could engage in safekeeping activities but also that state banks could do so. Certainly, there is a clear recognition in *Pattison* of the fact that safekeeping activities were being regularly performed by banks generally.⁷²

The second point is at least as important as the first. The invention of the safe deposit box created a new industry of safe deposit companies. These companies often took the form of

69. *Id.* at 704.

70. Redford, *Dual Banking: A Case Study in Federalism*, 31 LAW & CONTEMP. PROB. 749 (1966).

71. “[N]o distinction can be made in determining this question between a state and a National Bank.” *Pattison v. Syracuse Nat’l Bank*, 80 N.Y. 82, 90, 36 Am. Rep. 582, 584 (1880).

72. *Pattison v. Syracuse Nat’l Bank*, 80 N.Y. 82, 93, 36 Am. Rep. 582, 587 (1880).

safe deposit and trust companies. The *Pattison* court, in reviewing the facts giving rise to the controversy, made clear that for some time the Syracuse National Bank had engaged in safekeeping activities for its customers. It further made clear that before the particular deposit in dispute was made, "a trust company was formed in Syracuse for the receipt of valuables for safe-keeping, and that after the formation of that company . . . the cashier [decided] that they had better not take any more packages for safe-keeping . . ." ⁷³ In other words, it appears from the *Pattison* opinion that safe deposit and trust companies were beginning to be formed for the purpose of engaging in the safekeeping business and that they were competing directly with the banks.

E. The Beginning of Safe Deposit Activities in the United States

The *Graham* and *Pattison* cases and their forebears almost all indicate a recurrent fact pattern: a customer of the bank arrived with a package, usually in the form of an envelope, containing bonds, stocks, or other valuables; the cashier took these valuables, inventoried them, agreed to take them for safekeeping, and occasionally gave the customer a receipt for them; thereafter, the customer returned to the bank, only to find that the valuables were missing. There were variations on this theme, but invariably, once the valuables had been accepted for safekeeping by the bank, they were placed in the general vaults of the bank. Obviously, there were substantial risks involved for the customer. First, there was always the risk of the defalcating cashier. Second, there was the risk that, in transporting the envelopes containing the valuables from the vault to the customer or back to the vault, the envelope or its contents would be lost or misplaced. Additionally, a burglar who breached the security of the vault was, without more, capable of gaining possession of the securities. These risk factors, coupled with the development of the individual safe deposit box, led to the development of trust and safe deposit companies. Beginning in the mid-1860's, these compa-

73. *Id.* at 97, 36 Am. Rep. at 591.

nies, particularly in the urban areas, began to compete with, and in some cases displace, banks in their safekeeping function.

It must have been apparent to the bankers of the time that safe deposit boxes were likely to displace in large measure the safekeeping function of banks, for, as illustrated in the *Pattison* case, the existence of these companies served to discourage safekeeping by the banks. Logically, however, it made little sense for a bank customer to engage in safekeeping or safe deposit activities with a trust or safe deposit company, at least if that company could not offer other services as well. After all, the cases indicate that to a large extent safekeeping activities were carried on gratuitously. Moreover, banks already had vaults that were, if not impenetrable, at least quite strong. Beyond that, banks could offer safekeeping services in rural areas where it would not be economically feasible to establish a safe deposit company. Initially, banks likely viewed safe deposit companies as welcome adjuncts to the banking world, or perhaps viewed them with indifference, or at worst, as potential competitors. Over a period of years, however, two things must have become apparent: first, that banks, other than perhaps in urban areas, would continue to engage in safekeeping activities for their customers; and second, that people were willing to pay for safekeeping services. Therefore, banks could, by engaging in safe deposit activities, continue to serve their customers, and at the same time make (or at least not lose) money.

The banks were equipped for safekeeping services. The vaults existed, so it was merely a matter of constructing safe deposit facilities within a bank, or perhaps acquiring a safe deposit company. Once it became apparent that safe deposit activities could be conducted for a fee, that bank customers desired safe deposit or safekeeping services on a greater scale than had been undertaken in the past, that safekeeping could legally be undertaken without any question, and that independent safe deposit companies were not only being formed but were successful, it was only natural that banks would begin to engage in safekeeping and safe deposit activities to a much greater extent.

The period between 1880 and the early-1920's was a period of turmoil in the banking industry.⁷⁴ It was also, apparently, a period of extraordinary growth in the area of safe deposit and safekeeping services. Oddly enough, it was also a period of remarkable calm in the judicial development of legal rules relative to safekeeping and safe deposit activities. However, while the courts were not confronted with the question of whether banks could engage in safekeeping or safe deposit activities during this period, the legislatures of the various states were prevailed upon to pass legislation permitting safekeeping and safe deposit activities. It was in the latter part of the 19th century and the early part of the 20th century that state statutory enactments either recognized that banks and trust companies were engaged in safe deposit activities, or explicitly conferred the power to engage in safekeeping and safe deposit activities upon these institutions. Thus, Paton's Digest, beginning in 1926, listed a significant number of jurisdictions which "expressly authorized one or more kinds of banking institutions to receive special deposits or conduct a safe deposit business or have given statutory recognition to the right of banks to conduct such business"⁷⁵ The statutory recognition existed primarily in tax statutes which set requirements for the opening of safe deposit boxes following a decedent's death.⁷⁶

The passage of these statutes in numerous states following the *Graham* decision suggests a legislative attempt (spurred by the banks' lobbying efforts) to head off litigation concerning the question of whether state banks had authority to engage in safe deposit activities. The thought may well have been that, given the indications from the *Graham* case concerning the relationship between state and national banks, as well as the history behind the National Currency Act, which suggested equality between the two types of banks, legislative pronouncements with respect to state banks would be

74. J. WHITE, *THE REGULATION AND REFORM OF THE AMERICAN BANKING SYSTEM* 25 (1983).

75. 2 PATON'S DIGEST § 4191(2) (1926).

76. See MINN. STAT. § 2282 (1913); N.D. COMP. LAWS ch. 225 (1919); N.Y. BANKING LAW § 106(5) (McKinney 1921); MASS. GEN. LAWS ANN. ch. 79 (West 1921).

effective with respect to national banks as well. In any event, for one reason or another, the passage of the statutes apparently forestalled litigation concerning the entire question of whether banks—state or national—could engage in safe deposit activities.

However, other questions concerning the safekeeping and safe deposit functions were regularly litigated during that time. Indeed, such important questions as whether the contents of a safe deposit box could be reached by garnishment or attachment, the standard of care applicable to a bank involved in safe deposit activities, and related liability questions were litigated during this period.⁷⁷ But, as was the case with safekeeping for the fifty-year period between the *Essex* and *Wiley* decisions, the ultimate question of whether a bank could engage in safe deposit activities was not litigated at all.

The lack of litigation on this issue might well have signaled that banks were not engaged, to any large extent, in the safekeeping or safe deposit function. However, the evidence is to the contrary. First, the existence of the state statutes authorizing the conduct of a safe deposit or safekeeping function suggests legislative reaction to an existing phenomenon. Second, in the 1926 edition of Paton's Digest, Paton responds to an inquiry concerning the power of state and national banks to engage in safe deposit activities. The question—whether a state or national bank has the power to conduct safe deposit activities, absent statutory authority, either through a safe deposit department or a separate safe deposit company—is answered affirmatively, although cautiously. The digest, in an opinion dated 1924, reports that the question has never been squarely ruled upon, but the author goes on to state: "In view of the extent to which banks are now taking over the safe deposit business, the probability is it will be held the operation of such a business is within the power of a bank."⁷⁸

77. *Botton v. Clarke*, 7 Cush. 487 (Mass. 1851); *Jones v. Morgan*, 90 N.Y. 4, 43 Am. Rep. 131 (1882); *Safe Deposit Co. v. Pollock*, 85 Pa. 391, 27 Am. Rep. 660 (1877); *Mayer v. Brensinger*, 180 Ill. 110, 54 N.E. 159 (1899); *State v. Kelsey*, 53 N.J.L. 590, 22 A. 342 (1891). See also Lord, *The Relationship Between The Bank and its Safe Deposit Customer*, 5 CAMP. L. REV. 263 (1983).

78. 1 PATON'S DIGEST § 4189 (1926).

Those cases which dealt with banks and safe deposit activities in the period between 1880 and the 1920's did not address the question of a bank's authority to engage in safe deposit activities, primarily for the reason that bank counsel did not seek to avoid liability on the basis of *ultra vires*. Having won the right to engage in safekeeping activities in *Graham* (while at the same time losing the ability to claim *ultra vires*), it would have been disingenuous for the banks, which were beginning to conduct safe deposit activities on a large scale, to construct vaults or purchase safe deposit companies and then attempt to contend that their having done so was beyond their corporate power. It was one thing for the banks to claim *ultra vires* with respect to safekeeping; after all, the vaults were in existence, the safekeeping activity was undertaken as an accommodation for the customer in most cases, and the procedures used by the banks in safekeeping were, if not haphazard, by no means rigorously institutionalized. The safe deposit activities, on the other hand, were by their nature different. In order to engage in safe deposit activities, the bank had to affirmatively construct safe deposit vaults for safe deposit boxes, or purchase safe deposit companies with the vaults and boxes already constructed. Beyond that, having expended sums of money to engage in safe deposit activities, the banks had to charge a fee to their customers for safe deposit box use. The service could no longer be conducted gratuitously, although it was by no means a profit-making function.⁷⁹ Finally, because the customer played a role in safe deposit box access, institutional access procedures had to be developed. It was no longer sufficient for bank officers to retreat to the vault alone, pick up the valuables of the customer, and allow the customer to examine them. Rather, the customer had to accompany the officer, use his key for access along with the officer's, and was then entitled to examine the contents in private. These three factors, among others, would almost certainly preclude an assertion by the bank that safe deposit activities were *ultra vires*.

In fact, the determination of the question of whether a

79. McBain, *Safe Deposit Procedures*, 70 *BANKING L.J.* 242 (1953).

national bank could engage in safe deposit activities arose in a rather peculiar context. The banks which sought to escape liability for safekeeping losses on the basis of lack of corporate power were asserting that they were legally entitled to engage in safe deposit activities and, as nationally chartered entities, they were immune from state and local taxation with regard to those activities.

Given the fact that state banks were generally permitted to engage in safe deposit activities, as well as the fact that national banks were actively involved in safe deposit activities by the time that the two leading cases were decided, it is not surprising that the outcome of the cases permitted national banks to engage in safe deposit activities. It is, however, somewhat surprising that it took nearly sixty years following *Graham* for the controversies to arise.

The first case to consider the question, *Bank of California v. City of Portland*,⁸⁰ involved a dispute between three national banks and the City of Portland, Oregon, which had enacted a license tax on the conduct of safe deposit businesses. In 1935, the City of Portland assessed license fees against the three national banks based upon their operation of safe deposit vaults. (The licensing ordinance had existed in Portland since 1921, but it is not clear whether the banks had paid the tax in the past.) The banks objected to the payment of the license tax on the basis that they were national banks, chartered by the federal government, and were therefore immune from taxation as instrumentalities of the federal government so long as they were engaged in business pursuant to their charters. In other words, if conducting a safe deposit business were part of the business of banking, and if national banks were subject solely to regulation by the federal government, as instrumentalities of the federal government, the state or local governments could not legitimately tax them. Thus, the question as to whether conducting safe deposit activities was incidental to the business of banking was squarely presented. The Supreme Court of Oregon agreed with the national banks that it was incidental to the business of banking and further agreed that,

80. 157 Or. 203, 69 P.2d 273 (1937), *cert. denied*, 302 U.S. 765 (1938).

as a result, the banks were immune from state or local taxation.

The court noted initially that there were no precedents on point and that its decision would therefore have to be guided by analogy. It then sought to find an appropriate source of law beyond the analogical precedents of special deposits (including *Essex* and its progeny) and determined that it was appropriate to look to banking custom and history. Noting that fifty, and even one hundred years earlier, the arguments raised with regard to safe deposit boxes had been raised with respect to safekeeping and the taking of special deposits generally, the court referred to *Pattison* and the historical underpinnings of banking, both of which suggested that safekeeping of some kind had existed for centuries. The only real question then became whether safekeeping could be undertaken through the use of safe deposit boxes, as opposed to the general vaults of a bank. Perhaps most critical to the court's decision was the fact that, contained within a proviso to section 24 of the National Bank Act,⁸¹ there was express permission to invest in the capital stock of a safe deposit company. Given that, coupled with the testimony adduced at trial that national banks operated safe deposit facilities throughout the United States, the court had no difficulty reaching its conclusion: "The operation of safe deposit vaults by national banks is within the incidental powers granted to such banks by Congress and therefore is not ultra vires."⁸²

Other language in the *City of Portland* case suggests that the result might not have been the same had the case arisen significantly earlier in time. Thus, the court stated:

Time was, perhaps, when the safe deposit vault business would not be considered an integral part of the banking business, but in this day and age, as the testimony shows, the modern bank is not complete without safe deposit facilities, just as in earlier times the business of banking would have failed in one of its most important phases if the practice of receiving valuables for safekeeping had

81. 12 U.S.C. § 24 (1982).

82. *Bank of Cal. v. City of Portland*, 157 Or. 203, —, 69 P.2d 273, 277 (1937), cert. denied, 302 U.S. 765 (1938).

been eliminated.⁸³

The proviso to section 24 which permitted banks to invest in state safe deposit companies conclusively demonstrated to the court that banks not only conducted safe deposit facilities but that Congress was aware of that fact and had provided banks an alternative method for doing so:

This language recognizes the fact which Congress knows, which every banker knows, and which the courts and public know, that such safe-deposit business is being carried on by every important national bank in the entire country. This proviso was not a grant of an exclusive power, forbidding the exercise of the power in any other manner, but rather it is an extension of the power to conduct a safe-deposit business, an alternative method.⁸⁴

A similar issue came before the United States Supreme Court three years later, this time concerned with the legality of a Colorado state law which imposed a tax, payable by the banks, on the users of safe deposit boxes. The case, *Colorado National Bank v. Bedford*,⁸⁵ suggests that the Supreme Court of Oregon may have been incorrect with respect to its decision on the tax issue;⁸⁶ it left little doubt, however, that the Oregon high court had rendered the correct decision with respect to the safe deposit function of banks.

In the *Bedford* case, a Colorado state statute imposed a tax equal to two percent of the value of services that were performed by banks. According to the statute, the tax was to be paid by the bank but was to be passed on to the user or consumer of the service to the extent practicable. The Colorado National Bank operated a safe deposit department, and the two percent tax was assessed against the safe deposit services rendered. The bank refused to make payment, and the state sought a declaratory judgment with respect to the validity of the tax statute. The bank alleged that safe deposit activities were incidental to the business of banking pursuant to its national charter and therefore were immune from state taxa-

83. *Id.* at —, 69 P.2d at 279.

84. *Id.*

85. 310 U.S. 41 (1940).

86. *See id.* at 51-53.

tion. The trial court ruled in favor of the bank initially but was reversed by the Colorado Supreme Court. The trial court then found for the state and was affirmed.

The United States Supreme Court affirmed the decision of the Colorado Supreme Court. The Court, after satisfying itself that jurisdiction existed, premised its remarks on the assumption that national banks could exercise only those powers conferred upon them by Congress.⁸⁷ The Court then quoted the incidental powers clause of section 24 of the National Bank Act, as well as the safe deposit proviso, which permitted national banks to invest in state safe deposit companies. The Court noted that national banks were permitted to accept special deposits and then stated its belief that the acceptance of special deposits

differs little if at all from a safe-deposit business. The language of the proviso . . . is the language suitable to impose restrictions on a recognized power, not the language that would be used in creating a new power. . . . [T]he banks' own investment in safety deposit facilities evidently did not seem to Congress to require the same regulation as the purchase of stock in a safe-deposit corporation. A subsidiary safe-deposit corporation would give priority to the creditors of the subsidiary over the depositors and other creditors of the bank itself. The obvious fact, known to all, is that national banks do and for many years have carried on a safe-deposit business. State banks, quite usually, are given the power to conduct a safe-deposit business. We agree with the appellant bank that such a generally adopted method of safeguarding valuables must be considered a banking function authorized by Congress.⁸⁸

Thus, for the first time, the Supreme Court of the United States ruled on the question of whether a national bank could engage in the safe deposit business. The Court's reasoning was threefold: safe deposit activities were not significantly distinct from safekeeping activities; Congress had recognized that banks engaged in safe deposit activities and permitted

87. *Id.* at 48.

88. *Id.* at 49-50. On the role this case played in the development of the "business of banking," see Symons, *supra* note 28, at 711-12.

them to do so through subsidiary safe deposit companies; and banks had engaged in safe deposit activities so that custom, in and of itself, might justify recognition of the power to engage in safe deposit activities.

F. Present Authority to Engage in Safekeeping and Safe Deposit Activities

Based on the *City of Portland* and *Bedford* cases, it is now well settled that national banks may engage in safe deposit activities. With respect to state banks, the precise issue of whether a state bank may engage in safe deposit activities is governed by the statutes creating and regulating those banks. In many jurisdictions, the state statutory scheme specifically provides for the authority to engage in safe deposit activities.⁸⁹ In others, the authority is not granted specifically, but rather it exists as a result of an incidental powers clause similar to that in section 24 of the National Bank Act,⁹⁰ or a statute which permits state banks to do all that national banks may do.⁹¹ Finally, in a few jurisdictions, there is at best implied authority where reference is made to safe deposit boxes in other state enactments such as tax, will-search, or unclaimed-property statutes, thus suggesting legislative recognition of an ongoing practice.⁹² It remains possible in such a state for a court to declare safe deposit activities beyond the power of a state bank. However, in view of the history behind safe deposit activities, the implications which exist by virtue of references in other state statutes to safe deposit boxes, and the extent to which safe deposit activities are currently being performed by all banks—state and national—such a declaration would be highly improbable.

89. See, e.g., ALA. CODE § 5-5A-18(11) (Repl. 1981); ARIZ. REV. STAT. ANN. § 6-184 (Supp. 1974); COLO. REV. STAT. § 11-9-102 (Supp. 1983); GA. CODE § 7-1-261(2) (Supp. 1984); ILL. ANN. STAT. ch. 17, § 309 (Smith-Hurd 1981); MASS. GEN. LAWS ANN. ch. 168, § 69 (West 1977).

90. See, e.g., ALA. CODE § 5-5A-18(11) (Repl. 1981); MD. FIN. INST. CODE ANN. § 3-206 (1980); 1984 LA. ACTS. 719, § 1; N.C. GEN. STAT. § 53-43(1) (Repl. 1982); WYO. STAT. § 13-2-101 (1977).

91. See, e.g., ARIZ. REV. STAT. ANN. § 6-184 (Supp. 1974); N.D. CENT. CODE § 6-03-38 (Repl. 1975).

92. See ALA. CODE § 5-5A-18(11) (Repl. 1981); D.C. CODE ANN. § 26-401 (1981).

IV. AUTHORITY TO ENGAGE IN SAFE DEPOSIT ACTIVITIES THROUGH A SUBSIDIARY OR AFFILIATE

No discussion of the authority of banks to engage in safekeeping and safe deposit activities would be complete without discussing the fact that a substantial number of banks engage in safe deposit activities through safe deposit subsidiaries or affiliates. As the history of safe deposit activities suggests, the development of the modern safe deposit vault occurred in the mid-19th century as a result of the invention of the safe deposit box that required two keys for access. This invention led to the development of a new business—the safe deposit company. It was this historical accident that strengthened the argument that safe deposit activities were not a necessary adjunct to the business of banking, for if non-banks could and did engage in this type of activity, surely it was not an activity solely within the province of banks. Nevertheless, and while banks eventually overcame the competitive challenge presented by the safe deposit companies, it became quite clear that institutions other than banks could safekeep customer valuables.

As is often the case with competitors, the adage, “if you can’t beat them, join them,” began to make some sense. Thus, to the extent that safe deposit companies were ever a serious competitive force, the banks began to seek to absorb them. Moreover, it became clear to a number of bank attorneys that separate corporate entities provided insulation from the extraordinary potential liability that might result from safekeeping or safe deposit activities. With legislation in a number of states authorizing formation of safe deposit companies, it became a relatively common practice to form a safe deposit company to perform safe deposit activities on the premises of the bank. All that remained was to ensure that such activities were lawful.

Beginning in 1924, Congress considered the issue of whether national banks could engage in safe deposit activities through affiliates. Paton’s Digest reports that, in that year, a bill was introduced that would have permitted national banks to invest in safe deposit corporations located on or adjacent to

bank premises, up to an amount equal to fifteen percent of the bank's capital and surplus.⁹³ The bill is reported to have passed the House in early 1925 but failed in the Senate. Almost two years thereafter, in February 1927, Congress passed the proviso to section 24.⁹⁴

The legislative history behind the proviso reveals virtually nothing about why it was enacted. As has been seen, national banks had actively engaged in safe deposit activities on their premises for a number of years. What little information currently exists suggests that national banks were expanding their activities through the use of separate corporate entities. Thus, it is likely that congressional action mirrored developments within the industry, rather than the industry seeking congressional approval before beginning to conduct business in that particular manner.

This conclusion is suggested very strongly by the 1924 edition of Paton's Digest. The digest reports that no case authority existed at the time directly authorizing national banks to form a separate safe deposit company. Paton, however, suggests that such activity would likely be permissible in view of analogical precedents. Furthermore, in another portion of the digest, Paton sets forth a provision from the New York statute which quite clearly contemplated and permitted the formation of independent safe deposit companies.⁹⁵ That statute, section 106 of the New York banking law, permitted banks to purchase safe deposit stock so long as the safe deposit company was doing business on premises owned or leased by the bank and provided further that the board of directors first authorized the purchasing and holding of that stock.⁹⁶

Paton advised incorporation of a safe deposit company, with ownership of the stock primarily in the bank, in order to limit the liability of the bank. He concluded that "the advantage of incorporation would be that in case of a large loss the liability of the company would be limited to the assets and capital liability of the safe deposit company and not involve

93. 1 PATON'S DIGEST § 4190 (1926).

94. 12 U.S.C. § 24 (1982).

95. 2 PATON'S DIGEST § 4192(a) (1926).

96. *Id.* (quoting N.Y. BANKING LAW § 106(5) (McKinney 1921)).

the bank.”⁹⁷ Oddly enough, what gave rise to this advice was “the uncertainty of the law upon the question of liability”⁹⁸ caused by lack of clarity as to what would constitute reasonable care.⁹⁹

Given the fact that New York was undoubtedly the leading commercial state at the turn of the century, and the fact that Paton’s Digest was perhaps the most authoritative and heavily relied upon research tool of bank counsel, there is no doubt but that a substantial number of banks in New York incorporated safe deposit companies and purchased their stock. What remained unclear was whether it could be done by national banks. Congress, following the lead of New York, determined in 1927 that it could be.

The proviso to section 24 states:

That in carrying on the business commonly known as the safe-deposit business the association shall not invest in capital stock of a corporation organized under the law of any State to conduct a safe-deposit business in an amount in excess of 15 per centum of the capital stock of the association actually paid in and unimpaired and 15 per centum of its unimpaired surplus.¹⁰⁰

Thus, in 1927, it was made clear for the first time that national banks could engage in the safe deposit business through safe deposit subsidiaries.

As was indicated earlier, the language of the proviso played a large part in convincing the United States Supreme Court in the *Colorado National Bank* case that conducting safe deposit business was incidental to the business of banking. In footnote 22 of that case, the Court cites the legislative history of the proviso and indicates that Congress clearly perceived safe deposit activities as part of the legitimate business of banking. The House report, referred to by the Court, made clear that “[t]his is a business which is regularly carried on by national banks and the effect of this provision is also primarily

97. 2 PATON’S DIGEST § 4192(a) (1926).

98. *Id.*

99. See Lord, *The Legal Relationship Between the Bank and Its Safe Deposit Customer*, 5 CAMP. L. REV. 263 (1983).

100. 12 U.S.C. § 24(7) (1982).

regulative."¹⁰¹ That report, of course, bolsters the notion that this type of activity was going on throughout the early part of the twentieth century, and that Congress merely recognized it in the mid-1920's.

Since the passage of the proviso, banking has developed and changed forms many times. Thus, today, much of the business of banking is conducted through bank holding companies. It becomes important, therefore, to consider the extent to which a bank holding company may engage in safe deposit activities through an affiliate or subsidiary.

Obviously, a bank owned by a bank holding company could engage in safe deposit activities directly. And, it could do so itself by purchasing shares of the safe deposit company pursuant to section 24. However, for good reason, the bank holding company may prefer to independently acquire a safe deposit company so that the safe deposit company can conduct business as a subsidiary or affiliate of the holding company, not directly as a subsidiary of the bank. That it may do so is made explicitly clear by the Bank Holding Company Act.

Section 1843 of title 12 of the United States Code limits the activities of bank holding company subsidiaries to businesses that are closely related to banking. Section 1843(C) states that despite prohibitions on certain activities,

such prohibitions shall not, with respect to any other bank holding company, apply to—

(1) shares of any company engaged or to be engaged solely in one or more of the following activities: . . .

(B) Conducting a safe-deposit business¹⁰²

In other words, under the Bank Holding Company Act, bank holding companies may invest without limit in safe deposit companies. This section appears to be a recognition of the fact that safe deposit activities are "so closely related to banking . . . as to be a proper incident thereto."¹⁰³

101. *Colo. Nat'l Bank v. Bedford*, 310 U.S. 41, 50 n.22 (1940).

102. 12 U.S.C. § 1843(c) (1982).

103. *Id.*

V. CONCLUSION

The history of safe deposit activities in the United States suggests that originally banks engaged in safekeeping activities notwithstanding that they lacked authority to do so. They did so primarily for customer convenience, and, if the cases are to be believed, eventually regretted having done so. The banks themselves fostered substantial debate concerning the legitimacy of the safekeeping function when they were asked to bear responsibility for losses of customer property. When it became apparent that they could not escape liability for these losses on the basis of *ultra vires*, the banks continued to do that which they had always done: safekeep customers' valuables.

At that point, however, they encountered a new challenge, that created by the safe deposit companies which began to be formed in the mid-1800's. With the invention of the safe deposit box, the banks for the first time could engage in safekeeping and yet provide the customer with privacy. Safe deposit companies began to be formed to take advantage of the expanded market for keeping individual's valuables. Ultimately, for a variety of historic reasons, the banks began to engage in safe deposit activities in competition with the safe deposit companies and eventually fully supplanted them in all but the major urban markets. Unfortunately, it was not clear that banks had the authority to lease safe deposit boxes.

Beginning around the turn of the century, the states led the way in developing legislation which clearly permitted the banks to engage in safe deposit activities, in reality merely recognizing what the banks had been doing for years. In the mid-1920's, Congress authorized banks to engage in safe deposit activities through subsidiaries, though there was still no explicit authority to engage in safe deposit activities through a department within the bank itself. In the late-1930's, the Supreme Court of the United States finally ruled that banks did indeed have the power to engage in safe deposit activities, on the ground that such activities were necessary to the business of banking.

Today, virtually all banks have safe deposit departments. These departments are authorized not only to national banks

through Supreme Court edict and congressional implication, but also to state banks through a variety of state statutes. Moreover, banks are permitted to engage in safe deposit activities through affiliates or subsidiaries, the stock of which is owned by the bank or through subsidiaries owned by a bank holding company under the Bank Holding Company Act.

The history of safe deposit activities in the United States is in many ways reflective of the history of numerous other aspects of the banking industry and commercial law in this country.¹⁰⁴ As has been generally true, the law in this area followed and developed as a result of commercial practice. The banks, without clear authority to do so, undertook to provide a service demanded by their customers. When it was to their advantage to do so, they denied the ability to engage in the activity and therefore disclaimed responsibility for loss occasioned by it. And when it was to their advantage to be able to engage in the specified activity, they urged it as their right. The courts and legislatures eventually recognized it as a legitimate activity and regulated it appropriately.

But the history of safe deposit activities is more than of mere historical importance. Today, as much or more than at any time in the history of our country, the banking and other commercial industries are faced with new challenges caused by innovations and market pressures. To the extent that they meet these challenges as they have in the past, *i.e.*, by addressing them in a commercial manner regardless of their actual authority to do so, the courts and other regulators can deal with problems as they arise in a manner consistent with historical antecedents.¹⁰⁵ By recognizing that commercial practice often gives birth to regulation, and not vice versa, the courts and other regulators can permit the development of needed commercial devices yet govern those devices appropriately.

104. See generally Symons, *supra* note 28, at 714-26.

105. *Id.*